

not present or is not present in amounts sufficient to require submission of the schedules, or because the information required is included in the consolidated financial statements, including the notes thereto.

### 3. Index to Exhibits.

<TABLE>

<CAPTION>

EXHIBIT NO.

Description

<S>

<C>

3.1	Articles of Incorporation of the Company, (incorporated by referen Exhibit 3.1 to the Current Report on Form 8-K, no. 0-27658, filed June 30, 1997)
3.2	Articles of Amendment to Articles of Incorporation of the Company (creating Class B Senior Redeemable Preferred Stock) (incorporated reference to Exhibit C of Exhibit 10.35 below)
3.3	Bylaws of the Company, as amended (incorporated by reference to Ex 3.2 to the Current Report on Form 8-K, No. 0-27658, filed on June 1997)
3.4	Articles of Amendment to Articles of Incorporation filed August 14 2000 (incorporated by reference to Exhibit 3 to the Quarterly Repo filed on Form 10-Q, No. 027658, for the quarter ended September 30 2000)
4.1	Reference is hereby made to Exhibits 3.1, 3.2, 3.3 and 3.4
10.1*	Preferred Networks, Inc. 1994 Stock Option Plan (incorporated by reference to Exhibit 10.1 to the Registration Statement filed on F S-1, No. 33-80507)
10.2*	Preferred Networks, Inc. 1992 Stock Option Plan (incorporated by reference to Exhibit 10.2 to the Registration Statement filed on F S-1, No. 33-80507)
10.3(1)**	Preferred Networks, Inc. 1995 Stock Option Plan, as amended (incorporated by reference to Exhibit B to the Company's definitiv Proxy Statement on Form 14A filed on April 22, 1997)
10.3(2)**	Preferred Networks, Inc. 1995 Stock Option Plan, as amended (incorporated by reference to Exhibit A to the Company's definitiv Proxy Statement on Form 14A filed on April 29, 1998)
10.4*	Preferred Networks, Inc. 1995 Employee Stock Purchase Plan (incorporated by reference to Exhibit 10.4 to the Registration Statement filed on Form S-1, No. 33-80507)
10.5*	Preferred Networks, Inc. 1995 Non-Employee Directors' Restricted S Award Plan (incorporated by reference to Exhibit 10.5 to the Registration Statement filed on Form S-1, No. 33-80507)
10.6	Purchase Agreement dated June 21, 1995, among the Company, Fleet E Partners VI, L.P., Fleet Venture Resources, Inc., Chisholm Partner L.P., Centennial Fund IV, L.P., Saugatuck Capital Company Limited Partnership III, Primus Capital Fund III Limited Partnership, PNC Capital Corp. and certain of the Company's stockholders (incorpora by reference to Exhibit 10.6 to the Registration Statement filed o Form S-1, No. 33-80507)

</TABLE>

&lt;PAGE&gt; 24

&lt;TABLE&gt;

<S>	<C>
10.7	Stockholders Agreement dated June 21, 1995, among the Company, Fleet Equity Partners VI, L.P., Fleet Venture Resources, Inc., Chisholm Partners II, L.P., Centennial Fund IV, L.P., Saugatuck Capital Company Limited Partnership III, Primus Capital Fund III Limited Partnership PNC Capital Corp. and certain of the Company's stockholders (incorporated by reference to Exhibit 10.7 to the Registration Statement filed on Form S-1, No. 33-80507)
10.8	Registration Rights Agreement dated June 21, 1995 among the Company, Fleet Equity Partners VI, L.P., Fleet Venture Resources, Inc., Chisholm Partners II, L.P., Centennial Fund IV, L.P., Saugatuck Capital Company Limited Partnership III, Primus Capital Fund III Limited Partnership PNC Capital Corp. and certain of the Company's stockholders (incorporated by reference to Exhibit 10.8 to the Registration Statement filed on Form S-1, No. 33-80507)
10.9	Warrant to Purchase Common Stock dated June 22, 1995 issued to Leg Mason Wood Walker, Incorporated (incorporated by reference to Exhibit 10.9 to the Registration Statement filed on Form S-1, No. 33-80507)
10.10	Promissory Note and Credit Agreement dated April 1, 1995, between the Company and Glenayre Electronics, Inc. as amended (incorporated by reference to Exhibit 10.10 to the Registration Statement filed on Form S-1, No. 33-80507)
10.11	Credit Agreement and Promissory Note, each dated June 16, 1995, between the Company and Motorola, Inc. (incorporated by reference to Exhibit 10.11 to the Registration Statement filed on Form S-1, No. 33-80507)
10.12	Sublease Agreement, dated May 8, 1995, between the Company and The Carter Group for office space in Oakbrook Research Center, Norcross, Georgia (incorporated by reference to Exhibit 10.12 to the Registration Statement filed on Form S-1, No. 33-80507)
10.13	Lease Agreement and Addendum, dated October 14, 1992, between the Company and Connecticut Mutual Life Insurance Company for office space at Goshen Springs Road, Norcross, Georgia, as amended (incorporated by reference to Exhibit 10.13 to the Registration Statement filed on Form S-1, No. 33-80507)
10.14*	Management Employment Agreement, dated July 8, 1995, between the Company and Mark H. Dunaway (incorporated by reference to Exhibit 10.14 to the Registration Statement filed on Form S-1, No. 33-80507)
10.15*	Management Employment Agreement, dated July 7, 1995, between the Company and Michael J. Saner (incorporated by reference to Exhibit 10.15 to the Registration Statement filed on Form S-1, No. 33-80507)
10.16*	Management Employment Agreement, dated August 16, 1995, between the Company and Eugene H. Kreeft (incorporated by reference to Exhibit 10.16 to the Registration Statement filed on Form S-1, No. 33-80507)
10.17	Amendment No. 1, dated as of December 12, 1995, to Purchase Agreement dated June 21, 1995 among the Company, Fleet Equity Partners VI, L.P., Fleet Venture Resources, Inc., Chisholm Partners II, L.P., Centennial Fund IV, L.P., Saugatuck Capital Company Limited Partnership III, Primus Capital Fund III Limited Partnership, PNC Capital Corp. and certain of the Company's stockholders (incorporated by reference to Exhibit 10.17 to the Registration Statement filed on Form S-1, No. 33-80507)
10.18	Amendment No. 1, dated as of December 12, 1995, to Stockholders Agreement dated June 21, 1995 among the Company, Fleet Equity Partners VI, L.P., Fleet Venture Resources, Inc., Chisholm Partners II, L.P.

Centennial Fund IV, L.P., Saugatuck Capital Company Limited Partne III, Primus Capital Fund III Limited Partnership, PNC Capital Corp certain of the Company's stockholders (incorporated by reference t Exhibit 10.18 to the Registration Statement filed on Form S-1, No. 33-80507)

- 10.19 Lease Agreement, dated August 4, 1993, between Alamac Limited Partnership and the Company, as amended (incorporated by reference Exhibit 10.19 to the Registration Statement filed on Form S-1, No. 33-80507)
- 10.20 Sub-Lease Agreement, dated as of December 18, 1995 between PSB Bui Corp. and the Company (incorporated by reference to Exhibit 10.20 the Registration Statement filed on Form S-1, No. 33-80507)
- 10.21 Commercial Lease Contract, dated December 6, 1995, between Lantrac Investments, LLC and the Company (incorporated by reference to Exh 10.21 to the Registration Statement filed on Form S-1 No. 33-80507)
- 10.22 Promissory Note and Credit Agreement, dated January 26, 1996, betw the Company and Glenayre Electronics, Inc. (incorporated by refere to Exhibit 10.22 to the Registration Statement filed on Form S-1, 33-80507)

</TABLE>

24

<PAGE> 25

<TABLE>

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<C>

- 10.23 Letter Confirming Line of Credit with Associates Capital Services Corporation (incorporated by reference to Exhibit 10 to the Quarte Report filed on Form 10-Q, No. 0-27658, for the quarter ended Marc 1996)
- 10.24 Agreement and Plan of Merger, dated July 3, 1996, by and among Pag Services, Inc., Preferred Networks, Inc., and the shareholders of Paging Services, Inc. (incorporated by reference to Exhibit 10.1 t Quarterly Report filed on Form 10-Q, No. 0-27658, for the quarter June 30, 1996)
- 10.25 Credit Agreement dated August 8, 1996, by and among Preferred Netw Inc., PNI Systems, LLC, and NationsBank, N. A. (South) (incorporat reference to Exhibit 10.2 to the Quarterly Report filed on Form 10 No. 0-27658, for the quarter ended June 30, 1996)
- 10.26 Asset Purchase Agreement, dated as of June 19, 1996 and amended as September 5, 1996 and as of September 13, 1996, by and among Big A Paging Corporation, Preferred Networks, Inc. and Gary Hencken (incorporated by reference to the exhibit to the Current Report fi on Form 8-K, No. 0-27658, dated September 27, 1996)
- 10.27 Stock Purchase Agreement by and among Preferred Networks, Inc., Me Paging & Communications, Inc., HTB Communication, Inc., Custom Pag Inc., and M.P.C. Distributors Inc. (collectively, "Sellers") and t Shareholders of Sellers dated September 30, 1996 (incorporated by reference to Exhibit 10.3 to the Quarterly Report filed on Form 10 No. 0-27658, for the quarter ended September 30, 1996)
- 10.28 Agreement and Plan of Merger by and among Preferred Networks, Inc. Acquisition Corp., EPS Wireless, Inc. and the Shareholders of EPS Wireless, Inc. (incorporated by reference to Exhibit 2.1 to the Cu Report on Form 8-K, No. 0-27658, filed December 17, 1996)
- 10.29 First Amendment to Credit Agreement dated as of December 20, 1996, and among Preferred Networks, Inc., PNI Systems, LLC, and NationsB N.A. (South) (incorporated by reference to Exhibit 10.29 to the An Report on Form 10-K, No. 0-276548, filed on April 15, 1997)

- 10.30            Second Amendment to Credit Agreement dated as of March 12, 1997, b among Preferred Networks, Inc., PNI Systems, LLC, and NationsBank, (South) (incorporated by reference to Exhibit 10.30 to the Annual Report on Form 10-K, No. 0-276548, filed on April 15, 1997)
  
- 10.31            Commitment Letter dated April 9, 1997 between the Company, Centenn Fund IV, L.P., Saugatuck Capital III, PNC Capital Corp., Fleet Equ Partners, and Primus Venture Fund III (incorporated by reference t Exhibit 10.31 to the Annual Report on Form 10-K, No. 0-276548, fil April 15, 1997)
  
- 10.32            Third Amendment to Credit Agreement dated as of April 11, 1997, by among Preferred Networks, Inc., PNI Systems, LLC, and NationsBank, (South) (incorporated by reference to Exhibit 10.31 to the Annual Report on Form 10-K, No. 0-276548, filed on April 15, 1997)
  
- 10.33            Class A Redeemable Preferred Stock Purchase Agreement dated as of 21, 1997, by and among the Company and Centennial Fund IV, L.P., Saugatuck Capital Company Limited Partnership III, PNC Capital Cor Fleet Venture Resources, Inc., Fleet Equity Partners VI, L.P., Chi Partners II, L.P. and Primus Capital Fund III Limited Partnership (incorporated by reference to Exhibit A to the Company's definitiv Proxy Statement on Schedule 14A, filed May 22, 1997)
  
- 10.34            Agreement and Plan of Merger, dated May 21, 1997, by and between Preferred Networks, Inc. and PNI Merger Corp. (incorporated by reference to Exhibit B to the Company's definitive Proxy Statement Schedule 14A, filed on May 22, 1997)
  
- 10.35            Class B Senior Redeemable Stock Purchase Agreement dated as of Mar 17, 1998, by and among the Company, Alta Communications VI, L.P., Comm S By S, LLC, Centennial Fund IV, L.P., PNC Capital Corp., Saugatuck Capital Company Limited Partnership III, Primus Capital III Limited Partnership, Fleet Equity Partners VI, L.P., Fleet Ven Resources, Inc., T/W Alfred W. Putnam GST Exempt, Anne L. Putnam, Edward B. Putnam, Custodian for Fitzgerald B. Putnam Under the Uni Transfers to Minor Act, Pennsylvania, Webbmont Holdings L.P., Spot Dog Farm, L.P., RTM, Inc., Mark H. and Marcia M. Dunaway, and John and Sylvia Hurley (incorporated by reference to the Company's Annu Report on Form 10-K for the 1997 fiscal year, filed on March 30, 1
  
- 10.36            Fourth Amendment to Credit Agreement dated as of March 19, 1998, b among Preferred Networks, Inc., PNI Systems, LLC, and NationsBank, (South) (incorporated by reference the Company's Annual Report on 10-K for the 1997 fiscal year, filed on March 30, 1998)
  
- 10.37            Amendment to Registration Rights Agreement dated as of June 16, 19 (incorporated by reference to Exhibit E of Exhibit A to the Compan definitive Proxy Statement on Schedule 14A, filed on May 22, 1997)

</TABLE>

<PAGE>    26

<TABLE>

- <S>            <C>
- 10.38            Second Amendment to Registration Rights Agreement dated as of Marc 1998 (incorporated by reference the Company's Annual Report on For 10-K for the 1997 fiscal year, filed on March 30, 1998)
  
- 10.39            Fifth Amendment to Credit Agreement and waiver dated as of Novembe 1998, by and among the Company, PNI Systems, LLC, and NATIONS BANK, N.A., as successor to NationsBank, N.A. (South) (incorporated by reference to the Quarterly Report filed on Form 10-Q, No. 0-27658, the quarter ended September 30, 1998)

- 10.40 Asset Purchase Agreement, dated as of April 19, 1999, by and among Wireless Services Operating Corporation, Preferred Technical Servi Inc., and the Company (incorporated by reference to Exhibit 27 to Quarterly Report filed on Form 10-Q, No. 0-27658, for the quarter March 31, 1999)
- 10.41 Amendment to Asset Purchase Agreement, dated as of May 20, 1999, b among Wireless Services Operating Corporation , Preferred Technica Services, Inc., and the Company (incorporated by reference to Exhi 2.2 to the Current Report on Form 8-K, No. 0-27658, filed on June 1999)
- 10.42 Agreement Concerning Amendment to Credit Agreement dated as of May 1999, by and among the Company, PNI Systems, LLC, NationsBank, N.A and the guarantors party thereto (incorporated by reference to Exh 2.3 to the Current Report on Form 8-K, No. 0-27658, filed on June 1999)
- 10.43 Modification Agreement by and between the Company and Associates Capital Services Corporation dated May 28, 1999 (incorporated by reference to Exhibit 2.4 to the Current Report on Form 8-K, No. 0-27658, filed on June 14, 1999)
- 10.44 Share Purchase Agreement between the Registrant and Celestica Corporation dated December 10, 1999 (incorporated by reference to Exhibit 2 to the Current Report on Form 8-K, No. 0-27658, filed on December 22, 1999)
- 10.45 Second Agreement Concerning Amendment to Credit Agreement dated as December 9, 1999 by and among PNI Systems, LLC, the Registrant and of America, N.A. (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K, No. 0-27658, filed on December 22, 1999)
- 10.46 Agreement Concerning Amendment to Credit Agreement dated as of Dec 9, 1999 by and between the Registrant and Glenayre Electronics, In (incorporated by reference to Exhibit 10.2 to the Current Report o Form 8-K, No. 0-27658, filed on December 22, 1999)
- 10.47 Modification Agreement #4 by and between the Company and Associate Capital Services Corporation dated September 29, 2000 (incorporate reference to the Quarterly Report filed on Form 10-Q, No. 027658, the quarter ended September 30, 2000)
- 21 Subsidiaries of the Company (incorporated by reference to the Comp Annual Report on Form 10-K for the 1999 fiscal year, filed on Marc 2000)
- 23.1 Consent of Grant Thornton LLP
- 23.2 Consent of Ernst & Young LLP

</TABLE>

\* Indicates management contract or compensation plan or arrangement.

(b) Reports on Form 8-K.

No reports on Form 8-K were filed during the last quarter of the period covered by this report

## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

## PREFERRED NETWORKS, INC.

Date: April 16, 2001

By: /s/ Mark H. Dunaway

-----  
Mark H. Dunaway  
Chief Executive Officer and Director  
(Principal Executive Officer)

Date: April 16, 2001

By: /s/ Kathryn Loev Putnam

-----  
Kathryn Loev Putnam  
Senior Vice President and Chief Financial Officer  
(Principal Financial Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Date: April 16, 2001

By: /s/ Mark H. Dunaway

-----  
Mark H. Dunaway  
Chief Executive Officer and Director  
(Principal Executive Officer)

Date: April 16, 2001

By: /s/ William H. Bang

-----  
William H. Bang  
Director

Date: April 16, 2001

By: /s/ John J. Hurley

-----  
John J. Hurley  
Director

Date: April 16, 2001

By: /s/ Kathryn Loev Putnam

-----  
Kathryn Loev Putnam  
Senior Vice President and Chief Financial Officer  
and Director  
(Principal Financial Officer)

27

&lt;PAGE&gt; 28

FINANCIAL STATEMENTS AND REPORTS OF  
INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS  
PNI TECHNOLOGIES, INC.  
(FORMERLY KNOWN AS PREFERRED NETWORKS, INC.)  
December 31, 1999 and 2000

F-1

&lt;PAGE&gt; 29

## Report of Independent Certified Public Accountants

The Board of Directors and Stockholders  
PNI Technologies, Inc.

We have audited the accompanying consolidated balance sheets of PNI Technologies, Inc. and subsidiaries as of December 31, 1999 and 2000, and the related consolidated statements of operations, changes in stockholders equity, and cash flows for the years ended December 31, 1999 and 2000. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted

in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of PNI Technologies, Inc. and subsidiaries as of December 31, 1999 and 2000, and the consolidated results of its operations and its cash flows for the years ended December 31, 1999 and 2000, in conformity with accounting principles generally accepted in the United States.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note C to the financial statements, the Company has experienced net losses of \$5,017,276 and \$8,294,501 for the years ended December 31, 1999 and 2000, respectively. Additionally, the Company's current liabilities exceeded its current assets by \$3,676,298 and the Company had a stockholders' deficit of \$9,520,341 at December 31, 2000. In February 2001, the Company has ceased to make required principal and interest payments to certain of its lenders, constituting a default under the loan agreements. These factors, amongst others raise substantial doubt about the Company's ability to continue as a going concern. Management's plans in regard to these matters are also described in Note C. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

/s/ GRANT THORNTON LLP

Atlanta, Georgia  
March 8, 2001

F-2

<PAGE> 30

#### REPORT OF INDEPENDENT AUDITORS

The Board of Directors and  
Stockholders PNI Technologies, Inc.

We have audited the consolidated statements of operations, changes in stockholders' equity, and cash flows of Preferred Networks, Inc. (now known as PNI Technologies, Inc.) for the year ended December 31, 1998. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Since the date of completion of our audit of the accompanying 1998 financial statements and initial issuance of our report thereon dated April 15, 1999, which report contained an explanatory paragraph regarding the Company's ability

to continue as a going concern, the Company, as discussed in Note E and Note G, has sold substantially all of the assets of two wholly-owned subsidiaries and paid off its credit facility. Therefore, the conditions that raised substantial doubt about whether the Company will continue as a going concern no longer existed at March 28, 2000.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated results of operations and its cash flows of Preferred Networks Inc. for the year ended December 31, 1998 in conformity with accounting principles generally accepted in the United States.

/s/ ERNST & YOUNG LLP

Atlanta, Georgia  
 April 15, 1999, except for Note E and G  
 as to which the date is March 28, 2000  
 <PAGE> 31

PNI Technologies, Inc.  
 (formerly known as Preferred Networks, Inc.)

CONSOLIDATED BALANCE SHEETS

December 31,

ASSETS

<TABLE>  
 <CAPTION>

	1999
	-----
<S>	<C>
CURRENT ASSETS	
Cash and cash equivalents	\$ 5,489,89
Accounts receivable, less allowance for doubtful accounts	
of \$392,731 and \$487,570 in 1999 and 2000, respectively	1,532,59
Inventory	723,88
Prepaid expenses	473,96
Other current assets	813,44
	-----
Total current assets	9,033,78
PROPERTY AND EQUIPMENT, net	14,926,47
OTHER ASSETS	
Goodwill, net	6,855,66
FCC licenses, net	8,146,51
Other long-term assets, net	180,30
	-----
	15,182,49
	-----
	\$ 39,142,75
	=====

</TABLE>

The accompanying notes are an integral part of these statements.

F-3

<PAGE> 32

PNI Technologies, Inc.  
 (formerly known as Preferred Networks, Inc.)

CONSOLIDATED BALANCE SHEETS - CONTINUED

December 31,

## LIABILITIES, REDEEMABLE PREFERRED STOCK, AND STOCKHOLDERS' EQUITY

<TABLE>  
<CAPTION>

&lt;S&gt;

## CURRENT LIABILITIES

- Accounts payable
- Accrued liabilities
- Accrued salaries
- State taxes payable
- Current portion of notes payable and capital lease obligations

Total current liabilities

NOTES PAYABLE AND CAPITAL LEASE OBLIGATIONS,  
less current portion

CLASS A PREFERRED STOCK, no par value, \$1.50 par shares liquidation preference and redemption price; 13,500,000 shares authorized, 10,000,000 shares issued and outstanding in 1999 and 2000 (including \$3,808,333 and \$5,308,333 of undeclared dividends in 1999 and 2000, respectively)

CLASS B SENIOR REDEEMABLE PREFERRED STOCK, no par value, \$1.50 per share liquidation preference and redemption price; 5,500,000 shares authorized 5,333,336 shares issued and outstanding in 1999 and 2000 (including \$2,285,180 and \$3,829,079 of undeclared dividends in 1999 and 2000, respectively)

Total liabilities and redeemable preferred stock

## STOCKHOLDERS' EQUITY (DEFICIT)

- Preferred stock, no par value, 16,500,000 shares authorized; none issued and outstanding
- Common stock, no par value, 100,000,000 shares authorized; 16,369,302 and 16,520,417 shares issued and outstanding in 1999 and 2000, respectively
- Accretion of Class A and Class B Redeemable Preferred Stock
- Accumulated deficit

&lt;/TABLE&gt;

The accompanying notes are an integral part of these statements.

F-4

&lt;PAGE&gt; 33

PNI Technologies, Inc.  
(formerly known as Preferred Networks, Inc.)

## CONSOLIDATED STATEMENTS OF OPERATIONS

Years ended December 31,

<TABLE>  
<CAPTION>1998  
-----

<S>	<C>
Revenues	
Network services	\$ 13,204,172
Pager sales	6,171,898
Equipment revenue	--
Other services	190,777
	-----
Total revenues	19,566,847
Costs of revenues	
Network services	8,612,145
Pager sales	6,245,636
Equipment cost of revenue	--
Other services	--
	-----
Total costs of revenues	14,857,781
	-----
Gross margin	4,709,066
Selling, general and administrative expenses	9,818,215
Other expenses (income)	--
Impairment loss	--
Depreciation and amortization	6,094,758
	-----
Operating loss	(11,203,907)
Interest expense	(2,010,178)
Interest income	351,384
	-----
Net loss from continuing operations before income tax benefit and discontinued operations	(12,862,701)
Income tax benefit	--
	-----
Net loss from continuing operations	(12,862,701)
Discontinued operations	
Operating loss from discontinued operations	(2,328,734)
Gain on disposal of subsidiaries, net of taxes of \$5,123,000	--
	-----
Income (loss) from discontinued operations	(2,328,734)
Cumulative effect of change in accounting principle, net of tax benefit of \$623,000	--
	-----
Net Loss	(15,191,435)

&lt;/TABLE&gt;

The accompanying notes are an integral part of these statements.

F-5

&lt;PAGE&gt; 34

PNI Technologies, Inc.  
(formerly known as Preferred Networks, Inc.)

CONSOLIDATED STATEMENTS OF OPERATIONS - CONTINUED

Years ended December 31,

<TABLE>  
<CAPTION>

1998

<S>	<C>	<C>
Accretion of redeemable preferred stock	(583,062)	
Redeemable preferred stock dividend requirements	(2,445,161)	(2
	-----	----
Net loss attributable to common stock	\$ (18,219,658)	\$ (8
	=====	=====
Net loss per share of common stock		
Loss from continuing operations before cumulative effect of change in accounting principle	\$ (0.98)	\$
Income (loss) from discontinued operations	(0.14)	
Cumulative effect of change in accounting principle	--	
	-----	----
	\$ (1.12)	\$
	=====	=====
Weighted average number of common shares used in calculating net loss per share of common stock	16,257,586	16
	=====	=====
Pro forma net loss assuming accounting principle is applied retroactively	\$ (14,984,144)	\$ (3
Pro forma net loss attributable to Common Stock assuming change in accounting principle is applied retroactively	\$ (18,012,367)	\$ (6
Pro forma net loss per share	\$ (1.11)	\$

&lt;/TABLE&gt;

The accompanying notes are an integral part of these statements.

F-6

&lt;PAGE&gt; 35

PNI Technologies, Inc.  
(formerly known as Preferred Networks, Inc.)

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

Years ended December 31,

<TABLE>  
<CAPTION>

	Common Stock (\$ .0001 Par)	Additional Paid-in Capital	Common Stock (No par)	Acc Re Pr
	-----	-----	-----	----
<S>	<C>	<C>	<C>	<C>
Balance at December 31, 1997	\$ --	\$ --	\$ 62,900,973	\$
Accretion of Class A Redeemable Preferred Stock	--	--	--	
Undeclared dividends on Class A Redeemable Preferred Stock (\$0.15 per share)	--	--	(1,500,000)	
Accretion of Class B Redeemable Preferred Stock	--	--	--	
Undeclared dividends on Class B Redeemable Preferred Stock (\$0.18 per share)	--	--	(945,161)	
Issuance of common stock warrants	--	--	810,000	
Exercise of options	--	--	192,878	
Net loss	--	--	--	
	-----	-----	-----	----

Balance at December 31, 1998	--	--	61,458,690	
Accretion of Class A Redeemable Preferred Stock	--	--	--	
Undeclared dividends on Class A Redeemable Preferred Stock (\$0.15 per share)	--	--	(1,500,000)	
Accretion of Class B Redeemable Preferred Stock	--	--	--	
Undeclared dividends on Class B Redeemable Preferred Stock (0.18 per share)	--	--	(1,340,019)	
Issuance of 34,925 shares of common stock pursuant to employee stock purchase plan	--	--	9,277	
Vesting of 21,000 shares to Directors	--	--	15,750	
Net loss	--	--	--	
	----	----	-----	---
Balance at December 31, 1999	--	--	58,643,698	(
Accretion of Class A Redeemable Preferred Stock	--	--	--	
Undeclared dividends on Class A Redeemable Preferred Stock (\$0.15) per share)	--	--	(1,500,000)	
Accretion of Class B Redeemable Preferred Stock	--	--	--	
Undeclared dividends on Class B Redeemable Preferred Stock (\$0.18 per share)	--	--	(1,543,899)	
Vesting of 12,000 shares to Directors	--	--	12,000	
Exercise of options	--	--	294,181	
Net loss	--	--	--	
	----	----	-----	---
Balance at December 31, 2000	\$ --	\$ --	\$ 55,905,980	\$ (
	====	====	=====	===

&lt;/TABLE&gt;

The accompanying notes are an integral part of this statement.

F-7

&lt;PAGE&gt; 36

PNI Technologies, Inc.  
(formerly known as Preferred Networks, Inc.)

## CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended December 31,

<TABLE>  
<CAPTION>

	1998
	-----
<S>	<C>
Cash flows from operating activities:	
Net loss	\$(15,191,435)
Adjustments to reconcile net loss to net cash used in operating activities:	
Operating loss from discontinued operations	2,328,734
Depreciation and amortization	6,094,758
(Gain) loss on disposal of property and equipment	(38,951)
Impairment loss	--
Maintenance services from sale of PTS	--
Gain on disposal of subsidiaries	--

Cumulative effect of change in accounting principle	--
Bad debt expense	413,756
Stock option compensation expense	66,323
Changes in operating assets and liabilities:	
Accounts receivable	326,903
Inventory	(351,628)
Prepaid expenses and other current assets	(45,837)
Accounts payable	699,599
Accrued liabilities	218,450
Accrued salaries	(280,859)
	-----
Net cash used in continuing operating activities	(5,760,187)
Net cash provided by (used in) discontinued operations	(1,150,298)
	-----
Net cash used in operating activities	(6,910,485)
Cash flows from investing activities:	
Purchases of equipment	(263,584)
Purchases of equipment for discontinued operations	(506,125)
Purchase of other assets and FCC licenses	(432,398)
Net proceeds from sale of subsidiary	--
	-----
Net cash (used in) provided by investing activities	(1,202,107)

&lt;/TABLE&gt;

F-8

&lt;PAGE&gt; 37

PNI Technologies, Inc.  
(formerly known as Preferred Networks, Inc.)

## CONSOLIDATED STATEMENTS OF CASH FLOWS - CONTINUED

Years ended December 31,

<TABLE>  
<CAPTION>

	1998
	-----
<S>	<C>
Cash flows from financing activities:	
Proceeds from borrowings	1,450,000
Payments of borrowings	(1,847,906)
Issuance of Redeemable Preferred Stock	6,983,656
Issuance of common stock upon exercise of stock options	126,555
Issuance of common stock warrants	810,000
	-----
Net cash provided by (used by) financing activities of continuing operations	7,522,305
Net cash used by financing activities of discontinued operations	--
	-----
Net cash provided by (used by) financing activities	7,522,305
Net decrease in cash and cash equivalents	(590,287)
Cash and cash equivalents, beginning of year	6,607,446
	-----
Cash and cash equivalents, end of year	\$ 6,017,159
	=====
Cash paid during year for	
Interest	\$ 2,010,773
Income taxes	\$ --

&lt;/TABLE&gt;

## Supplemental Cash Flow Information

During 1998 and 2000, the Company purchased property and equipment of approximately \$229,000 and \$200,000, respectively, through the issuance of notes payable and under capital leases. No such purchases were made in 1999.

The accompanying notes are an integral part of these statements.

F-9

&lt;PAGE&gt; 38

PNI Technologies, Inc.  
(formerly known as Preferred Networks, Inc.)

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 1999 and 2000

## NOTE A - NATURE OF OPERATIONS

## 1. Nature of Operations

PNI Technologies, Inc. formerly known as Preferred Networks, Inc. (the "Company") provides outsourcing services to the wireless industry primarily in the United States. The Company commenced operations in 1991 as a carrier's carrier of one-way paging networks, whereby the Company's customers purchase and resell the Company's network services to their subscribers. In July 1996, the Company acquired Preferred Technical Services, Inc. ("PTS"), a provider of wireless network equipment installation, maintenance and engineering services. This subsidiary was sold during 1999. In December 1996, the Company acquired EPS Wireless, Inc. ("EPS"), a national provider of paging and cellular product repair services, sales of new, used and refurbished paging and cellular products and inventory management services. This subsidiary was sold during 1999. During 1999, the Company completed development of its intelligent, high-speed switching technology. The Company shipped its first beta units in 1999 and has limited revenues in 2000. With the introduction of its networking products, the Company is evolving into a developer and supplier of advanced communications hardware and software products. However, the Company is at an early stage of development of its networking products business and substantially all of its revenues and costs continue to be derived from its network services business. The Company changed its name effective August 2000.

## NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Company's significant accounting policies are summarized as follows:

## 1. Accounting Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

## 2. Principles of Consolidation

The Company has formed wholly-owned subsidiaries and limited liability companies to execute certain business transactions. All significant intercompany activity has been eliminated.

F-10

&lt;PAGE&gt; 39

PNI Technologies, Inc.  
(formerly known as Preferred Networks, Inc.)

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 1999 and 2000

## NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

## 3. Revenue Recognition

The Company recognizes revenue on network services when the service is provided. Revenue from the sale of pagers, cellular products and networking products is recognized when the related product is shipped. Other service revenue consists primarily of miscellaneous fees charged to Direct Access Customers related to maintenance of customer equipment at Company TCC's. No one customer provided more than 10% of revenue during 1998, 1999 and 2000.

The Securities and Exchange Commission ("SEC") issued Staff Accounting Bulletin ("SAB") 101, Revenue Recognition in financial Statements, in December 1999. SAB 101 summarizes certain of the SEC staff's views in applying accounting principles generally accepted in the United States to revenue recognition in financial statements. The Company reviewed its revenue recognition policies and determined that they are in compliance with SAB 101.

## 4. Cash and Cash Equivalents

The Company considers short-term investments with original maturity dates of 90 days or less at date of purchase to be cash equivalents. Short-term investments are carried at cost plus accrued interest, which approximates fair market value.

## 5. Concentration of Credit Risk

Financial instruments that potentially subject the Company to concentration of credit risk consist principally of cash equivalents and accounts receivable. Cash equivalents are held with two financial institutions. Accounts receivable represent trade receivables and are unsecured. The Company performs periodic credit evaluations of its customers' financial condition and generally does not require collateral to support customer receivables. The Company is at risk to the extent such amounts become uncollectible. The Company provides an allowance for doubtful accounts based on factors surrounding the credit risk of specific customers, historical trends, and other information. At December 31, 1999 and 2000, approximately 16% and 13%, respectively, of accounts receivable was with one customer.

## 6. Inventory

Inventory consists primarily of new pagers and parts for networking products at December 31, 2000. The amounts are stated at the lower of cost or market, with cost of new product and repair parts being determined under the first-in, first-out (FIFO) method and the cost of refurbished products being determined principally by use of the specific identification method. Inventory has been reduced to market value at both December 31, 1999 and 2000.

F-11

&lt;PAGE&gt; 40

PNI Technologies, Inc.  
(formerly known as Preferred Networks, Inc.)

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 1999 and 2000

## NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

## 7. Property and Equipment

Property and equipment, including items financed through notes payable and capital leases, is stated at cost. No interest was capitalized in 1998, 1999 and

2000. The Company depreciates its property and equipment over their estimated useful lives using the straight-line method for financial reporting purposes and accelerated methods for tax reporting purposes. Estimated useful lives range from five to seven years.

8. FCC Licenses

Federal Communications Commission ("FCC") licenses consist of costs associated with the purchases of licenses and license application fees. These amounts are being amortized over a 15-year period, using the straight-line method. Accumulated amortization at December 31, 1999 and 2000 totaled \$2,251,448 and \$2,944,760, respectively.

9. Goodwill

Goodwill represents the excess purchase price over the fair value of the assets acquired in various acquisitions. Goodwill is amortized using the straight-line method over 15 years. At December 31, 1999 and 2000, accumulated amortization was \$1,674,011 and \$2,242,656, respectively.

10. Other Assets

At December 31, 1998, other assets included deposits with creditors and market entry costs. In 1999, market entry costs in the amount of \$1,832,397 were expensed and included in the caption "cumulative effect of change in accounting principle" in accordance with the Accounting Standards Executive Committee's Statement of Position 98-5, Reporting on the costs of Start-Up Activities ("SOP 98-5"). At December 31, 1999 and 2000, other assets consist of deposits with creditors.

11. Impairment of Long-Lived Assets

Statement of Financial Accounting Standards ("SFAS") No. 121, Accounting For The Impairment Of Long-Lived Assets and For Long-Lived Assets To Be Disposed Of, requires impairment losses to be recognized for long-lived assets used in operations when indicators of impairment are present and the undiscounted cash flows are not sufficient to recover the assets' carrying amount. The impairment loss is measured by comparing the fair value of the asset to its carrying amount. In 1999, the Company recorded an impairment charge of \$1,339,909 related to the write down of certain assets located in geographical markets where the Company no longer intends to operate. In accordance with SFAS No. 121, the impairment charge was taken at the time the Company made the decision not to pursue its expansion plans to these markets, which was December 31, 1999. No impairment charge was recorded in 2000.

F-12

<PAGE> 41

PNI Technologies, Inc.  
(formerly known as Preferred Networks, Inc.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 1999 and 2000

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

12. Advertising Expenses

The Company expenses all advertising expenses as incurred. Advertising expense for the years ended December 31, 1998, 1999 and 2000 was \$17,105, \$7,861 and \$75,869, respectively.

13. Income Taxes

The Company accounts for income taxes using the asset and liability method. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial

statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates applied to taxable income. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is provided for deferred tax assets when it is more likely than not that the asset will not be realized.

14. Stock-Based Compensation

The Company accounts for its stock-based compensation plans under Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees. Effective in 1995, the Company adopted the disclosure option of Statement of Financial Accounting Standards ("SFAS") No. 123, Accounting for Stock-Based Compensation. SFAS No. 123 requires that companies that do not choose to account for stock-based compensation as prescribed by the statement, shall disclose the pro forma effects on earnings and earnings per share as if SFAS No. 123 had been adopted. Additionally, certain other disclosures are required with respect to stock compensation and the assumptions used to determine the pro forma effects of SFAS No. 123 (see Note J).

15. Net Loss Per Share

Net loss per share was computed using the requirements of Statement of Financial Accounting Standards No. 128, Earnings Per Share, and Staff Accounting Bulletin No. 98. Net loss per share-basic was computed by dividing net loss attributable to common stock by the weighted average number of shares of common stock outstanding during the period excluding unvested shares of restricted stock. The denominator for net loss per share-diluted also considers the dilutive effect of outstanding stock options, warrants, and convertible preferred stock. Due to the Company's net loss, the amounts reported for basic and diluted are the same. The following securities could potentially dilute basic earnings per share in the future and were not included in the computation of diluted net loss per share because they would have been antidilutive for the period presented:

F-13

<PAGE> 42

PNI Technologies, Inc.  
(formerly known as Preferred Networks, Inc.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 1999 and 2000

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

15. Net Loss Per Share - Continued

<TABLE>  
<CAPTION>

	1998	1999	2000
	-----	-----	-----
<S>	<C>	<C>	<C>
Common stock options	2,467,168	1,303,788	926,263
Common stock warrants	17,322,353	17,322,353	17,322,353
Unvested restricted stock	69,000	42,000	12,000
	-----	-----	-----
Total securities	19,858,521	18,668,141	18,260,616
	=====	=====	=====

</TABLE>

16. Use of Estimates

In preparing financial statements in conformity with generally accepted accounting principles, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of

contingent assets and liabilities as of the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

17. Fair Value of Financial Instruments

The Company's financial instruments include cash and cash equivalents and notes payable. Estimates of fair value of these instruments are as follows:

Cash and cash equivalents - The carrying amount of cash and cash equivalents approximates fair value due to the relatively short maturity of these instruments.

Notes payable - The carrying amount of the Company's notes payable approximate fair value based on borrowing rates currently available to the Company for borrowings with comparable terms and conditions.

18. Reclassifications

Certain amounts in the 1998 and 1999 financial statements have been reclassified to conform with the current year presentation.

F-14

<PAGE> 43

PNI Technologies, Inc.  
(formerly known as Preferred Networks, Inc.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 1999 and 2000

NOTE C - REALIZATION OF ASSETS

The accompanying financial statements have been prepared in conformity with generally accepted accounting principles, which contemplate continuation of the Company as a going concern. However, the Company has incurred a net loss of \$5,017,276 and \$8,294,501 for the years ended December 31, 1999 and 2000, respectively. In addition, at December 31, 2000, the Company's current liabilities exceed its current assets by \$3,676,298 and the Company continues to use, rather than provide, significant cash in its operations for each of the years ended December 31, 1999 and 2000. In February 2001, the Company has ceased to make required principal and interest payments to certain of its lenders, constituting a default under the loan agreements. The default allows the lenders to demand immediate payment of the entire principal balance and accrued interest on this debt.

In view of the matters described in the preceding paragraph, recoverability of a major portion of the recorded asset amounts shown in the accompanying balance sheet is dependent upon continued operations of the Company, which in turn is dependent upon the Company's ability to meet its financing requirements on a continuing basis, to maintain present financing, and to succeed in its future operations. The financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or amounts and classification of liabilities that might be necessary should the Company be unable to continue in existence.

In response to the matters described in the preceding paragraphs, management has explored a variety of financing and restructuring alternatives, including selling or licensing various assets and restructuring or reorganizing its outstanding debt and/or its business. In the absence of such an event, PNI would be required to explore implementing a plan of reorganization under U.S. Bankruptcy Code.

The Company operates in the wireless communications industry, which has experienced and continues to experience significant challenges including competing technologies, shifts in customers' strategies, changes in the FCC regulatory environment, and limited sources of capital. As a result, the Company

is continually required to address these and other matters in its business strategy and operations. Since its March 1996 initial public offering, the Company has invested approximately \$62 million in building its network infrastructure, acquiring FCC licenses and other paging networks, and acquiring related companies. As a result of this expansion and the development of the Company's business and the overall wireless industry, the Company has experienced net losses and negative cash flows, and future cash flows have been difficult to project.

F-15

<PAGE> 44

PNI Technologies, Inc.  
(formerly known as Preferred Networks, Inc.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 1999 and 2000

NOTE C - REALIZATION OF ASSETS - Continued

The outcome of the uncertainties surrounding the Company and the industry are difficult to predict. These uncertainties could affect the Company's ability to recover the carrying value of its long-lived assets from its future cash flows and operations. Currently, generally accepted accounting principles require companies to assess future cash flows and record impairment losses on long-lived assets based on estimates of future cash flows if insufficient to recover the carrying values. Should the Company's future projections not materialize, the Company could experience an impairment of its long-lived assets requiring a charge to its income statement. As of December 31, 2000, the Company had \$25 million in net book value of long-lived assets, including property and equipment, FCC licenses, and goodwill.

NOTE D - ADOPTION OF NEW ACCOUNTING STANDARD

In April 1998, the Accounting Standards Executive Committee issued Statement of Position 98-5, Reporting on the costs of Start-Up Activities ("SOP 98-5"). SOP 98-5 requires entities to charge to expense start-up costs, including organization costs, as incurred. In addition, SOP 98-5 requires a write-off of any previously capitalized start-up or organizational costs, to be reported as a cumulative effect of a change in accounting principle. The Company adopted SOP 98-5 effective January 1, 1999 and wrote off the unamortized amount of its market entry costs at January 1, 1999 in the amount of \$1,832,397.

NOTE E - DISCONTINUED OPERATIONS

On May 28, 1999, the Company sold substantially all of the assets of its wholly-owned subsidiary, Preferred Technical Services ("PTS"), a provider of wireless network equipment installation, maintenance and engineering services. Under the terms of the purchase agreement, the Company received \$3,088,625 in proceeds from the sale and a \$1 million credit for maintenance services to be provided by PTS to the Company on its paging networks. At December 31, 1999, approximately \$417,000 of this credit remained unused and was included as prepaid expenses in the accompanying consolidated balance sheet. This entire credit was used by the Company during 2000. The Company recognized a gain on the sale of PTS in the amount of \$1,187,928 in 1999. As the operations of this subsidiary represented a separate segment, operating results for this subsidiary for all periods presented have been reclassified and reported as discontinued operations in accordance with Accounting Principles Board Opinion No. 30.

On December 10, 1999, the Company sold its wholly-owned subsidiary EPS Wireless, Inc. ("EPS"), a provider of paging and cellular product repair services, sales of new, used and refurbished paging and cellular products and inventory management services. The Company received \$14.9 million in proceeds from this sale subject to a holdback of \$750,000. This holdback, which was included in other current assets at December 31, 1999, was received in full during 2000. The Company recognized a gain on the sale of EPS in the amount of \$7,448,532 in 1999. As the operations of this subsidiary represented a separate segment,

operating results for this subsidiary for all periods presented have been reclassified and reported as discontinued operations in accordance with Accounting Principles Board Opinion No. 30.

F-16

&lt;PAGE&gt; 45

PNI Technologies, Inc.  
(formerly known as Preferred Networks, Inc.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 1999 and 2000

NOTE E - DISCONTINUED OPERATIONS - Continued

Summary operating results of the discontinued network engineering and maintenance services segment and the pager and cellular product repair services, sales and inventory management segment are as follows:

<TABLE>  
<CAPTION>

	1998	19
	-----	-----
<S>	<C>	<C>
Revenue:		
Network engineering and maintenance	\$ 3,992,277	\$ 3,0
Product repair and sales	15,567,218	14,9
	-----	-----
	19,559,495	17,9
	-----	-----
Costs and expenses:		
Network engineering and maintenance	3,893,380	3,0
Product repair and sales	17,994,849	14,9
	-----	-----
	21,888,229	18,0
	-----	-----
Operating loss from discontinued operations	\$ (2,328,734)	\$ (1
	=====	=====

&lt;/TABLE&gt;

NOTE F - PROPERTY AND EQUIPMENT

Property and equipment consists of the following:

<TABLE>  
<CAPTION>

	1999	2000
	-----	-----
<S>	<C>	<C>
Network services equipment	\$ 22,202,480	\$ 21,912,038
Computer equipment	1,212,483	1,767,016
Other equipment	1,326,156	1,178,123
Vehicles	--	144,703
Furniture and fixtures	548,186	600,447
Construction in progress	1,813,642	1,813,642
Leasehold improvements	817,023	817,023
	-----	-----
	27,919,970	28,232,992
	(12,993,495)	(16,810,447)
	-----	-----
	\$ 14,926,475	\$ 11,422,545
	=====	=====

&lt;/TABLE&gt;

At December 31, 1999 and 2000 substantially all property and equipment is pledged as collateral under various notes payable and capital lease obligations. Depreciation expense was approximately \$3,951,932, \$3,822,466 and \$3,929,061 for the years ended December 31, 1998, 1999 and 2000, respectively.

F-17

&lt;PAGE&gt; 46

PNI Technologies, Inc.  
(formerly known as Preferred Networks, Inc.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 1999 and 2000

NOTE F - PROPERTY AND EQUIPMENT - Continued

Construction in progress represents equipment acquired, but not yet placed in service. The Company expects to utilize such equipment in its future operations, as the market condition and capital availability permit. These amounts are not being depreciated.

NOTE G - NOTES PAYABLE AND CAPITAL LEASE OBLIGATIONS

<TABLE>  
<CAPTION>

&lt;S&gt;

Revolving credit facility with a financial institution; maximum borrowings of \$2,000,000 at December 31, 2000, bearing interest at prime plus 2% (10.5% at December 31, 2000). Due and payable on March 31, 2001; secured by certain assets of the Company.

Line of credit with equipment manufacturer, maximum borrowings are outstanding at December 31, 2000, bearing interest at the rate of 12.57% at December 31, 2000.

Notes payable to finance company, bearing interest at the rate of 10%, payable in various monthly installments of principal and interest with maturity dates through 2003; secured by paging equipment.

Note payable to financial institution, bearing interest at 9%, payable in monthly installments of principal and interest through July 2005; secured by automobiles.

Amounts due under capital leases for equipment due in various monthly installments until 2005; secured by the related equipment.

Less current portion

Long-term debt

&lt;/TABLE&gt;

In December 1999, in conjunction with its sale of a subsidiary, the Company entered into a new revolving facility agreement, which allows for borrowings at the lesser of \$2,000,000 or the sum of 75% of eligible accounts receivable and eligible inventory up to \$500,000. The amount available under this facility at December 31, 2000 was \$7,000. The Company also amended its loan covenant requirements and as a result, the Company was in compliance with its single remaining loan covenant requiring a minimum cash balance of \$1.1 million at December 31, 2000. The agreement expires on March 31, 2001.

F-18

&lt;PAGE&gt; 47

PNI Technologies, Inc.  
(formerly known as Preferred Networks, Inc.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 1999 and 2000

NOTE G - NOTES PAYABLE AND CAPITAL LEASE OBLIGATIONS - Continued

In February 2001, the Company has ceased to make required principal and interest payments to certain of its lenders, constituting a default under the loan agreements. The default allows the lenders to demand immediate payment of the entire principal balance and accrued interest on this debt.

As of December 31, 2000, approximate future principal maturities of notes payable and capital lease obligations for each of the next five years are as follows:

<TABLE> <CAPTION> Year ended December 31, <S>		<C>
	2001	\$5,283,151
	2002	34,469
	2003	41,288
	2004	46,328
	2005	30,866
		-----
		\$5,436,102
		=====

&lt;/TABLE&gt;

NOTE H - STOCKHOLDERS' EQUITY

Preferred Stock

In June 1997, the Company issued 10.0 million shares of Class A Redeemable Preferred Stock (the "Class A Preferred") and warrants to purchase up to 11.5 million shares of common stock for a total purchase price of \$15.0 million. Dividends accrue at the rate of 10% per annum and are cumulative. The Class A Preferred may be redeemed at any time at the option of the Company at a price equal to \$1.50 per share plus accrued dividends. If the holder so demands and after redemption of the Class B Senior Redeemable Preferred Stock described below, five years from the date of issuance, the Class A Preferred must be redeemed by the Company at a price equal to \$1.50 per share plus accrued dividends. Each warrant is exercisable for five years following the issuance of the Class A Preferred and entitles the holder to purchase one share of common stock for \$1.50 per share subject to possible downward adjustment based on any private placement of the Company's preferred or common stock for less than \$1.50 per share. A portion of the warrants may be canceled by the Company in the event of an early redemption of all of the Class A preferred. The Class A preferred is recorded at cost, net of expenses, plus \$6,823,621 in undeclared dividends and accretion.

F-19

&lt;PAGE&gt; 48

PNI Technologies, Inc.  
(formerly known as Preferred Networks, Inc.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 1999 and 2000

## NOTE H - STOCKHOLDERS' EQUITY - Continued

## Class B Senior Redeemable Preferred Stock

In March 1998, the Company issued 5,333,336 shares of Class B Senior Redeemable Preferred Stock (the "Class B Preferred") and warrants to purchase up to 5.4 million shares of common stock for a total purchase price of \$8 million. Dividends accrue at the rate of 15% per annum, are cumulative and compound annually. The Class B preferred may be redeemed at any time at the option of the Company at a price equal to \$1.50 per share plus accrued dividends and if the holder so demands, five years from the date of issuance, the Class B Preferred must be redeemed by the Company at a price equal to \$1.50 per share plus accrued dividends. In the event of redemption of the Class A Preferred, the Company must simultaneously redeem the Class B Preferred. Each warrant is exercisable for five years following the issuance of the Class B Preferred and entitles the holder to purchase one share of common stock for \$1.50 per share subject to possible downward adjustment based on any private placement of the Company's preferred or common stock for less than \$1.50 per share. A portion of the warrants may be canceled by the Company in the event of an early redemption of all of the Class B Preferred. The Class B Preferred is recorded at cost, net of expenses, plus \$4,387,703 in undeclared dividends and accretion.

## Common Stock Warrants

In addition to the warrants issued in conjunction with the Class A Preferred and Class B Preferred described above, the Company has other warrants outstanding. At December 31, 2000, the Company had outstanding warrants to purchase up to 183,750 shares of common stock at \$1.50 per share, exercisable until November 15, 2009, and warrants to purchase 238,603 shares of common stock at \$4.24 per share, exercisable until June 2005.

## Restricted Stock

The Company has a Non-Employee Directors' Restricted Stock Award Plan which provides for awards of common stock to the non-employee directors upon election to the board or every five years. In 1999 and 2000, no shares were issued under this Plan. The Company is recognizing the expense related to this issuance over the vesting period, which ends in 2001. The related expense recognized was immaterial in all years. At December 31, 1999 and 2000, 42,000 and 12,000, shares were unvested, respectively.

## NOTE I - STOCK PLANS

As of December 31, 2000, the Company has five stock plans (the 1992, 1994, and 1995 Stock Option Plans, the 1995 Employee Stock Purchase Plan, and the 1995 Non-Employee Directors' Restricted Stock Award Plan). In 1994, the Board of Directors voted to discontinue the granting of any additional options under the 1992 Stock Option Plan.

F-20

&lt;PAGE&gt; 49

PNI Technologies, Inc.  
(formerly known as Preferred Networks, Inc.)

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 1999 and 2000

## NOTE I - STOCK PLANS - Continued

The Company has both incentive stock options and nonqualified stock options outstanding, with varying vesting schedules. As of December 31, 2000, 4,410,613 shares of common stock were reserved for issuance under the five plans, of which 3,484,377 were available for future option grants and restricted stock awards. A summary of the Company's stock option activity and related information is as follows:

<TABLE>  
<CAPTION>

	Number of shares underlying options	Range exercise p per sha
	-----	-----
<S>	<C>	<C>
Outstanding at December 31, 1997	1,705,989	\$0.97 - \$
Granted	1,256,601	\$0.69 - \$
Exercised	(95,774)	\$0.97 - \$
Forfeited	(307,982)	\$0.97 - \$
Canceled	(91,666)	\$2.13 - \$
	-----	-----
Outstanding at December 31, 1998	2,467,168	\$0.69 - \$
Granted	-	
Exercised	-	
Forfeited	(1,047,900)	\$0.69 - \$
Canceled	(115,480)	\$2.13 - \$
	-----	-----
Outstanding at December 31, 1999	1,303,788	\$0.69 - \$
Granted	-	
Exercised	(175,115)	\$0.69 - \$
Forfeited	(202,410)	\$0.69 - \$
Canceled	-	
	-----	-----
Outstanding at December 31, 2000	926,263	\$0.69 - \$

<CAPTION>

	Number of shares underlying options	Range of exercise pr per shar
	-----	-----
<S>	<C>	<C>
Exercisable at December 31, 1998	550,360	\$0.97 - \$10
	=====	=====
Exercisable at December 31, 1999	1,065,358	\$0.69 - \$ 2
	=====	=====
Exercisable at December 31, 2000	766,726	\$0.69 - \$ 2
	=====	=====

</TABLE>

F-21

<PAGE> 50

PNI Technologies, Inc.  
(formerly known as Preferred Networks, Inc.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 1999 and 2000

NOTE I - STOCK PLANS - Continued

Additional information regarding stock options by range of exercise prices as of December 31, 2000 is as follows:

<TABLE>  
<CAPTION>

	Options Outstanding			O
	Number of	Weighted Average	Weighted Average	
Exercise Price	Options	Exercise Price	Contract Life	Number
	-----	-----	-----	Optio

<S>	<C>	<C>	<C>	<C>
\$0.68 - \$0.97	126,992	\$ 0.72	6.95	55,3
\$1.50 - \$2.50	799,270	2.03	6.09	711,4
	-----	-----	-----	-----
Total or average	926,263	\$ 1.85	6.21	766,7
	=====	=====	=====	=====

</TABLE>

Pro Forma Information

Pro forma information regarding net earnings and earnings per share is required by FAS 123, which also requires that the information be determined as if the Company has accounted for its stock options granted subsequent to December 31, 1994 under the fair value method of that statement. The fair value for these options was estimated at the date of grant using a minimum value option valuation method for options granted prior to the IPO and a Black-Scholes option valuation model for options granted after the IPO with the following weighted-average assumptions for 1998: a risk-free interest rate of 5.64%; a dividend yield of 0%; volatility factor of the expected market price of the Company's common stock of 99%; and a weighted-average expected life of the option of 4 years. No options were granted in 1999 and 2000.

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options which have no vesting restrictions and are fully transferable. In addition, option valuation models requires the input of highly subjective assumptions including the expected stock price volatility. Because the Company's stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimates, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its stock options.

The weighted average fair value of options granted in 1998 is \$1.53 per share. No options were granted in 1999 and 2000.

For purposes of pro forma disclosures, the estimated fair value of the options is amortized to expense over the options' vesting period. The Company's pro forma information follows:

<TABLE>  
<CAPTION>

	1998	1999
	-----	-----
<S>	<C>	<C>
Pro forma net loss	\$ (16,028,422)	\$ (5,631,2
Pro forma net loss per share of common stock	\$ (1.17)	\$ (0.

</TABLE>

PNI Technologies, Inc.  
(formerly known as Preferred Networks, Inc.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED  
December 31, 1999 and 2000

NOTE J - INCOME TAXES

The components of income tax expense (benefit) from continuing operations are:

<TABLE>  
<CAPTION>

1998	1999	2000
------	------	------

<S>	<C>	<C>	<C>
Year ended December 31,			
Current - Federal	\$ --	\$ (4,000,000)	\$ --
Deferred	--	--	--
	----	-----	----
	\$ --	\$ (4,000,000)	\$ --
	====	=====	====

&lt;/TABLE&gt;

For the year ended December 31, 1999, income taxes have been allocated between continuing operations and other items in accordance with SFAS No. 109, Accounting for Income Taxes. The net loss from continuing operations includes the related tax benefit; remaining income taxes have been allocated to the cumulative effect of change in accounting principle and the gain on disposal of subsidiaries, including taxes related to approximately \$5,000,000 of non-deductible goodwill and \$500,000 of state taxes currently payable.

For the year ended December 31, 1999, net operating loss carryforwards of approximately \$1,700,000 were utilized to offset currently taxable income. Deferred tax assets arising from the net operating loss carryforwards have been fully offset by a valuation allowance as of December 31, 2000. As of December 31, 2000, the Company has net operating loss carryforwards of approximately \$62,000,000 for federal income tax purposes. Such carryforwards, which expire at various dates through 2020, could be available to reduce future federal taxable income subject to limitations resulting from substantial changes in the Company's ownership.

The significant components of the Company's deferred tax assets and liabilities are:

<TABLE>  
<CAPTION>

	1999	2000
	-----	-----
<S>	<C>	<C>
Deferred tax assets		
Net operating loss carryforwards	\$ 21,234,978	\$ 22,377,236
Accounts receivable allowance	149,081	185,082
Inventory reserves	67,476	50,204
Vacation accrual	36,161	20,291
Other	9,500	106,068
	-----	-----
	21,497,196	22,738,881
Valuation allowance	(19,569,543)	(21,243,631)
Deferred tax liabilities		
Accumulated depreciation	(1,927,653)	(1,495,250)
	-----	-----
Net deferred assets	\$ --	\$ --
	=====	=====

&lt;/TABLE&gt;

F-23

&lt;PAGE&gt; 52

PNI Technologies, Inc.  
(formerly known as Preferred Networks, Inc.)

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 1999 and 2000

NOTE J - INCOME TAXES - Continued

The net change in the valuation allowance for deferred tax assets was an increase (decrease) of \$5,990,069, \$(448,167) and \$1,674,088 in 1998, 1999 and 2000, respectively.

The reconciliation of income tax attributable to operations computed at the U.S. Federal statutory rates to income tax expense is:

<TABLE>  
<CAPTION>

	1998	1999	2000
	----	----	----
<S>	<C>	<C>	<C>
Tax at federal statutory rate	(34.0)%	(34.0)%	(34.0)%
State taxes, net of federal tax benefit	(4.0)	(4.0)	(4.0)
Nondeductible expenses	1.1	-	-
Effect of valuation allowance	36.9	4.0	38.0
	-----	-----	-----
	-%	(34.0)%	-%
	=====	=====	=====

</TABLE>

#### NOTE K - COMMITMENTS

The Company leases sites and other facilities for its transmitters, terminals and other equipment and also leases office space under noncancellable operating leases which expire at various dates. As of December 31, 2000, approximate minimum annual rental payments required by these operating leases are as follows:

<TABLE>  
<CAPTION>

Year ending December 31,	<C>
<S>	
2001	\$ 2,778,000
2002	1,078,000
2003	526,000
2004	386,000
2005	308,000
Thereafter	102,000
	-----
	\$ 5,178,000
	=====

</TABLE>

Rental expense for the years ended December 31, 1998, 1999 and 2000 was approximately \$3.6 million, \$3.6 million and \$3.3 million, respectively.

As of December 31, 2000, the Company had one letter of credit outstanding for \$53,000. This letter of credit expires in 2001, and is collateralized by a certificate of deposit of \$53,000.

F-24

<PAGE> 53

PNI Technologies, Inc.  
(formerly known as Preferred Networks, Inc.)

#### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 1999 and 2000

#### NOTE L - EMPLOYEE BENEFIT PLAN

The Company provides a 401(k) plan that provides retirement benefits to substantially all employees at least 21 years of age with at least 90 days of

continuous service. The Company is required to match 10% of each participant's contributions up to 1% of their salary or may make contributions at the discretion of the Board of Directors, subject to statutory limitations. The Company's contributions were not material in 1998, 1999 or 2000.

NOTE M - SEGMENT INFORMATION

In 1998, the Company's three reportable industry segments were: (i) one-way wireless networks, whereby companies purchase non-branded, wholesale network services from the Company for resale to their customers (through its PNI Access Services Division); (ii) network engineering and maintenance services, supporting one-way and two-way wireless technologies (through Preferred Technical Services, Inc.) and (iii) pager and cellular product repair services, product sales and inventory management and fulfillment through EPS Wireless, Inc.) These industry segments were all operating in separate, one hundred percent owned, subsidiaries. During 1999, the Company sold two of its subsidiaries and as a result, at December 31, 1999 and 2000, the Company is operating only through its PNI Access Services Division with the other previous year industry segments included as discontinued operations.

F-25

<PAGE> 54

Report of Independent Certified Public Accountants  
on Schedule II

Board of Directors  
PNI Technologies, Inc.

In connection with our audit of the consolidated financial statements of PNI Technologies, Inc. and Subsidiaries referred to in our report dated March 8, 2001, which is included in the annual report to security holders and incorporated by reference in Part II of this form, we have also audited Schedule II for the year ended December 31, 2000. In our opinion, the schedule presents fairly, in all material respects, the information required to be set forth therein as of and for the year ending December 31, 2000.

/s/ GRANT THORNTON LLP

Atlanta, Georgia  
March 8, 2001

F-26

<PAGE> 55

REPORT OF INDEPENDENT AUDITORS

The Board of Directors and Stockholders  
Preferred Networks, Inc.

We have audited the consolidated financial statements of Preferred Networks, Inc. (now known as PNI Technologies, Inc.) as of December 31, 1998, and for the year ended December 31, 1998, and have issued our report thereon dated April 15, 1999, except for Note E and Note G as to which the date is March 28, 2000. Our audit also included the financial statement schedule listed in Item 14 (a) of this Annual Report on Form 10-K. This schedule is the responsibility of the Company's management. Our responsibility is to express an opinion based on our audit.

In our opinion, the 1998 financial statement schedule referred to above, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

/s/ ERNST & YOUNG LLP

Atlanta, Georgia  
 April 15, 1999, except for Note E and G  
 as to which the date is March 28, 2000.  
 <PAGE> 56

## PNI Technologies, Inc.

## SCHEDULE II - VALUATION AND QUALIFYING ACCOUNTS

<TABLE>  
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Column A	Column B	Column C
Description	Balance at Beginning of Period	Additions Charged to Costs and Expenses
<S>	<C>	<C>
Year ended December 31, 2000		
Reserve and allowance deducted from		
Asset accounts		
Allowance for doubtful accounts	\$ 392,731	\$ 799,8
Valuation allowance of deferred taxes	19,569,543	1,674,0
Year ended December 31, 1999		
Reserve and allowance deducted from		
Asset accounts		
Allowance for doubtful accounts	\$ 241,844	\$ 395,9
Valuation allowance of deferred taxes	\$ 20,017,710	\$
Year ended December 31, 1998		
Reserve and allowance deducted from		
Asset accounts		
Allowance for doubtful accounts	\$ 553,080	\$ 413,7
Valuation allowance of deferred taxes	14,027,641	5,990,0

&lt;/TABLE&gt;

(1) - Bad Debt write offs.

(2) - Column C-2 "Charged to other accounts" has been omitted as the response is  
 "none".

F-27

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 <SEQUENCE>2  
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&lt;PAGE&gt; 1

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EXHIBIT 23.1

CONSENT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Directors  
 PNI Technologies, Inc.

We hereby consent to the incorporation by reference of our reports dated March 8, 2001, appearing in the Company's Annual Report on Form 10-K for the year ended December 31, 2000, in the Company's Registration Statements on Form S-8, file numbers 333-3962, 333-3824, 333-3826 and 333-33879.

/s/ GRANT THORNTON LLP

Atlanta, Georgia  
April 13, 2001

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EXHIBIT 23.2

#### CONSENT OF INDEPENDENT AUDITORS

We consent to the incorporation by reference in the Registration Statements (Form S-8 No. 333-3962, Form S-8 No. 333-3824, Form S-8 No. 333-3826 and Form S-8 No. 333-33879) of Preferred Networks, Inc. (now known as PNI Technologies, Inc.) and in the related Prospectuses of our reports dated April 15, 1999, except for Note E and Note G as to which the date is March 28, 2000, with respect to the 1998 consolidated financial statements and schedule of PNI Technologies, Inc. included in the Annual Report (Form 10-K) for the year ended December 31, 2000.

/s/ ERNST & YOUNG LLP

Atlanta, Georgia  
April 13, 2001

</TEXT>

</DOCUMENT>

**PNI TECHNOLOGIES INC**

**Filing Type:** 10-Q  
**Description:** Quarterly Report  
**Filing Date:** Aug 20, 2001  
**Period End:** Jun 30, 2001

**Primary Exchange:** Over the Counter Bulletin Board  
**Ticker:** PNLG



## Table of Contents

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*To jump to a section, double-click on the section name.*

### 10-Q OTHERDOC

PART I.....	2
Item 1.....	2
Balance Sheet.....	2
Table2.....	3
Income Statement.....	3
Cash Flow Statement.....	4
ITEM 2.....	8
Table5.....	8
ITEM 3.....	15
PART II.....	15
ITEM 1.....	15
ITEM 3.....	15
ITEM 6.....	15

1

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, DC 20549  
FORM 10-Q

(Mark One)

☒ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended: June 30, 2001

OR

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 0-27658  
PNI TECHNOLOGIES, INC.

(formerly Preferred Networks, Inc.)

(Exact name of Registrant as Specified in its Charter)

GEORGIA	58-1954892
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

850 Center Way, Norcross, GA 30071  
(Address of principal executive offices)  
(Zip Code)

(770) 582-3500  
(Registrant's telephone number including area code)

Not Applicable  
(Former name, former address and former fiscal year,  
if changed since last year)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes ☒ No ☐

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 16,520,417 shares of common stock, no par value, as of August 20, 2001.

2

PNI TECHNOLOGIES, INC.  
(DEBTOR-IN-POSSESSION)

INDEX TO FORM 10-Q

PART I. FINANCIAL INFORMATION  
PAGE

NUMBER

-----

Item 1. Financial Statements

	Condensed Consolidated Balance Sheets for June 30, 2001 (Unaudited) and December 31,	
2000.....		3
	Condensed Consolidated Statements of Operations for the three and six months ended June 30, 2001 and 2000	
(Unaudited).....		4
	Condensed Consolidated Statements of Cash Flows for the three and six months ended June 30, 2001 and 2000	
(Unaudited).....		5
	Notes to Condensed Consolidated Financial Statements	
(Unaudited).....		6
	Item 2. Management's Discussion and Analysis of Financial Condition and Results of	
Operations.....		9
	Item 3. Quantitative and Qualitative Disclosure of Market Risk.....	14

PART II. OTHER INFORMATION

	Item 1. Legal Proceedings.....	14
	Item 3. Defaults Upon Senior Securities.....	14
	Item 6. Exhibits and Reports on Form 8- K.....	18
Signatures.....		16

3

PNI TECHNOLOGIES, INC.  
(DEBTOR-IN-POSSESSION)

CONDENSED CONSOLIDATED BALANCE SHEETS

	JUNE 30, 2001 (UNAUDITED)	DECEMBER 31, 2000
ASSETS		
Current assets		
Cash and cash equivalents .....	\$ 1,207,741	\$ 1,912,625
Accounts receivable, net .....	652,429	1,562,409

Inventory .....	244,547	1,285,051
Prepaid expenses and other current assets .....	209,045	140,468
Total current assets .....	2,313,762	4,900,553
Property and equipment, net .....	3,213,263	11,422,545
Goodwill net .....	--	6,314,652
FCC licenses, net .....	--	7,454,935
Other assets, net .....	169,361	180,306
	<u>\$ 5,696,386</u>	<u>\$ 30,272,991</u>

LIABILITIES, REDEEMABLE PREFERRED STOCK,  
AND STOCKHOLDERS' DEFICIT

Current liabilities		
Pre-petition accounts payable .....	\$ 3,454,257	\$ 1,912,829
Post-petition accounts payable .....	135,002	--
Accrued liabilities .....	1,303,669	1,237,585
Accrued compensation .....	37,995	143,286
Current portion of notes payable and capital lease obligations .....	5,348,981	5,283,151
Class A Redeemable Preferred Stock, no par value, \$1.50 per share redemption price; 13,500,000 shares authorized, 10,000,000 shares issued and outstanding (including \$6,046,038 of undeclared dividends in 2001) .....	20,674,980	--
Class B Senior Redeemable Preferred Stock, no par value, \$1.50 per share redemption price; 5,500,000 shares authorized, 5,333,336 shares issued and outstanding (including \$3,829,079 of undeclared dividends in 2001) .....	12,327,150	--
Total current liabilities .....	43,282,034	8,576,851
Notes payable and capital lease obligations, less current portion .....	--	152,951
Class A Redeemable Preferred Stock, no par value, \$1.50 per share redemption price; 13,500,000 shares authorized, 10,000,000 shares issued and outstanding (including \$5,308,333 of undeclared dividends in 2000) .....	--	19,725,682
Class B Senior Redeemable Preferred Stock, no par value, \$1.50 per share redemption price; 5,500,000 shares authorized, 5,333,336 shares issued and outstanding (including \$4,685,190 and \$3,829,079 of undeclared dividends in 2001 and 2000, respectively) .....	--	11,371,349
Total liabilities and Redeemable Preferred Stock .....	43,282,034	39,826,833

Deficit in Stockholders' Equity

Common Stock, no par value, 100,000,000 shares authorized in 2001 and 2000; 16,520,417 issued and outstanding in 2001 and 2000, respectively .....	54,320,062	55,905,980
Accretion of Redeemable Preferred Stock .....	(2,385,195)	(2,073,912)
Accumulated deficit .....	(89,520,515)	(63,385,910)
Total Stockholders' deficit .....	(37,585,648)	(9,553,842)
	<u>\$ 5,696,386</u>	<u>\$ 30,272,991</u>

See notes to condensed consolidated financial statements.

3

PNI TECHNOLOGIES, INC.  
(DEBTOR-IN-POSSESSION)

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
(UNAUDITED)

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	2001	2000	2001	2000
Revenues				
Network services .....	\$ 1,957,992	\$ 2,712,071	\$ 4,106,670	\$ 5,648,672
Pager sales .....	558,904	791,190	1,039,978	1,610,025
Networking products .....	65,992	189,409	101,464	258,900
Other services .....	30,611	66,907	73,167	104,665
Total revenues .....	2,613,499	3,759,577	5,321,279	7,622,262
Costs of revenues				
Network services .....	1,670,682	1,839,401	3,456,483	3,818,421
Pager sales .....	501,251	664,350	972,909	1,383,972

Networking products .....	137,339	112,070	309,134	209,528
Other services .....	109	133	2,451	1,252
Total costs of revenues .....	2,309,381	2,615,954	4,740,977	5,413,173
Gross margin .....	304,118	1,143,623	580,302	2,209,089
Selling, general and administrative expenses .....	2,117,483	1,616,159	3,570,290	3,218,105
Reorganization costs .....	69,720	--	69,720	--
Depreciation and amortization .....	1,312,103	1,261,599	2,623,964	2,561,501
Impairment Loss .....	20,149,970	--	20,149,970	--
Operating loss .....	(23,345,158)	(1,734,135)	(25,833,642)	(3,570,517)
Interest expense .....	(151,074)	(162,333)	(304,698)	(325,506)
Interest income .....	540	75,111	3,735	101,128
Net Loss .....	(23,495,692)	(1,821,357)	(26,134,605)	(3,794,895)
Accretion of Redeemable Preferred Stock .....	(155,642)	(155,653)	(311,282)	(311,284)
Redeemable Preferred Stock dividend requirements .....	(823,866)	(719,989)	(1,593,816)	(1,444,717)
Net loss attributable to Common Stock .....	<u>\$(24,475,200)</u>	<u>\$ (2,696,999)</u>	<u>\$(28,039,703)</u>	<u>\$ (5,550,896)</u>
Net loss per share of Common Stock .....	\$ (1.48)	\$ (.16)	\$ (1.70)	\$ (.34)
Weighted average number of common shares used in: calculating net loss per share of Common Stock .....	16,520,417	16,544,417	16,520,417	16,472,917

See notes to condensed consolidated financial statements.

4

5

PNI TECHNOLOGIES, INC.  
(DEBTOR-IN-POSSESSION)

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(UNAUDITED)

	SIX MONTHS ENDED JUNE 30,	
	2001	2000
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss .....	\$(26,134,605)	\$ (3,794,895)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization .....	2,623,964	2,561,501
Maintenance services from sale of PTS .....	--	416,665
Bad debt expense .....	810,092	214,556
Impairment loss .....	20,149,970	--
Stock option and restricted stock grant compensation expense .....	7,898	23,254
Changes in operating assets and liabilities:		
Accounts receivable .....	99,888	(477,606)
Inventory .....	256,384	(222,002)
Prepaid expenses and other assets .....	(68,577)	8,628
Accounts payable .....	1,676,430	(421,158)
Accrued liabilities .....	91,084	81,608
Accrued compensation .....	(105,291)	(7,358)
Net cash used in operating activities .....	(592,763)	(1,616,807)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of equipment .....	--	(91,356)
Payment of accrued expenses related to sale of subsidiary in 1999 .....	--	(570,000)
Proceeds from holdback related to sale of subsidiary in 1999 .....	--	750,000
Purchases of other assets and FCC licenses .....	--	--
Net cash used by investing activities .....	--	88,644
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from borrowings .....	--	550,000
Repayments of borrowings .....	(112,121)	(999,482)
Issuance of redeemable preferred stock .....	--	--
Issuance of Common Stock upon exercise of stock options .....	--	290,746
Net cash provided (used) by financing activities .....	(112,121)	(158,736)
Net increase (decrease) in cash and cash equivalents .....	(704,884)	(1,686,899)

Cash and cash equivalents, beginning of period .....	1,912,625	5,489,898
Cash and cash equivalents, end of period .....	\$ 1,207,741	\$ 3,802,999

See notes to condensed consolidated financial statements.

5

6

PNI TECHNOLOGIES, INC.  
(DEBTOR-IN-POSSESSION)

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
JUNE 30, 2001  
(UNAUDITED)

1. THE COMPANY

PNI Technologies, Inc., formerly known as Preferred Networks, Inc. ("PNI" or the "Company"), commenced operations in 1991 as a carrier's carrier of one-way paging networks, whereby the Company's customers purchase and resell the Company's network services to their subscribers. During 1999, the Company completed development of its intelligent, high-speed switching technology. The Company shipped its first beta units in 1999 and in early 2000, began shipments to customers of its first networking products. However, substantially all of its revenues and costs continue to be derived from its network services business. Due to the early stages of commercial sales of PNI's networking products, PNI's limited working capital, and PNI's limited development personnel, PNI has been inhibited in its ability to complete multiple customer orders. Concurrent with its Chapter 11 Bankruptcy filing, PNI suspended all development, assembly and shipments of its networking products. PNI does not expect to resume such activities in the foreseeable future, although it may seek to transfer or license its patent with respect to these technologies. The Company changed its name effective August 2000.

2. BASIS FOR PRESENTATION

The interim condensed consolidated financial information contained herein has been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC") and includes in the opinion of management, all adjustments, which are of a normal recurring nature necessary for a fair presentation of the financial position, results of operations and cash flows for the periods presented. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles ("GAAP") have been condensed or omitted pursuant to such rules and regulations. The Company believes, however, that its disclosures are adequate to make the information presented not misleading. These financial statements and related notes should be read in conjunction with the financial statements and notes as of December 31, 2000, included in the Company's Annual Report on Form 10-K (File No. 0-27658) and the Company's Quarterly Report on Form 10-Q for the period ending March 31, 2001. Results of operations for the periods presented herein are not necessarily indicative of results to be expected for the full year or any other interim period.

3. CHAPTER 11 REORGANIZATION

On June 8, 2001 (the "Petition Date"), PNI Technologies, Inc. and all of its subsidiaries (collectively, the "Debtors"), filed voluntary petitions for relief under Chapter 11, Title 11 of the United States

Code (the "Bankruptcy Code") in the United States Bankruptcy Court for the Northern District of Georgia (the "Bankruptcy Court"). The Debtors are managing their business as "debtor-in-possession" in accordance with the applicable provisions of the Bankruptcy Code. No trustee or examiner has been appointed to the cases.

Subsequent to the commencement of the Chapter 11 cases, the court has approved certain orders which were intended to enable the Debtors to continue business operations as debtors-in-possession. To date, the most significant of these orders (i) permitted the Debtors to utilize cash collateral, with the consent of the Company's senior lender, for its continuing operations (consisting of the majority of its network operations in the Southeast and Northeast) during the Chapter 11 cases in substantially the same manner as it was operated prior to the commencement of the Chapter 11 cases; (ii) authorized the Debtors to discontinue service in certain markets (consisting of its networks in the Mid-west, Florida, the Mid-Atlantic and selected networks operating on certain frequencies in the Southeast and Northeast); (iii) authorized payment of post-petition wages, vacation pay, and employee benefits and reimbursement of employee business expenses; (iv) authorized payment of pre and post-petition regulatory fees and taxes, including franchise, personal property, net worth, capital and gross receipts taxes owed by the Debtors; and (v) authorized the Debtors to pay certain pre-petition obligations to critical vendors to aid the Debtors in maintaining operation of their businesses.

6

7

PNI TECHNOLOGIES, INC.  
(DEBTOR-IN-POSSESSION)

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
JUNE 30, 2001  
(UNAUDITED)

In bankruptcy, the rights of, and the Debtors' ultimate payments to, pre-petition creditors and shareholders may be substantially altered. This could result in claims being liquidated in the bankruptcy cases at less (and possibly substantially less) than 100% of their face value, and the equity of the Debtors' common shareholders being diluted or cancelled. In addition, pursuant to the provisions of the Bankruptcy Code, the Debtors are not permitted to pay any claims or obligations that arose prior to the Petition Date ("Pre-petition Claims") unless specifically authorized by the Bankruptcy Court. Similarly, claimants may not enforce any claims against the Debtors that arose prior to the Petition Date unless specifically authorized by the Court. The Debtors also have the right, as debtors-in-possession, subject to the Bankruptcy Court's approval, to assume or reject any executory contracts and unexpired leases in existence on the Petition Date. Parties having claims as a result of such rejection may file claims with the Court, which will be addressed as part of the Chapter 11 cases. The Bankruptcy Code also provides that the Debtors have an exclusive period during which only they may propose and file and solicit acceptances of a plan of reorganization. This period may be extended upon request of the Debtors and subsequent Bankruptcy Court approval. If the Debtors fail to file a plan of reorganization during the exclusive period, as extended, or, after such plan has been filed, if the Debtors fail to obtain acceptance of such plan from the requisite classes of creditors and equity security holders during the exclusive solicitation period, any party in interest may file their own plan of reorganization for the Debtors.

Due to material uncertainties, it is not possible to determine the additional amount of claims that may arise or ultimately be filed, or to predict the length of time the Debtors will operate under the

protection of Chapter 11 of the Bankruptcy Code, the outcome of the bankruptcy cases in general, whether the Debtors will continue to operate under their current organizational structure, or the effect of the cases on the Debtors' business or on the claims and interests of the various creditors and security holders.

Although the Chapter 11 bankruptcy filing raises substantial doubt about the Company's ability to continue as a going concern, the accompanying financial statements have been prepared on a going-concern basis. This basis contemplates the continuity of operations, realization of assets, and discharge of liabilities in the ordinary course of business. With the exception of certain assets written down pursuant to an impairment loss (as further discussed in Management's Discussion and Analysis of Financial Condition and Results of Operations below), the statements also present the assets of the Company at historical cost. A plan of reorganization could materially change the amounts and the carrying values currently disclosed in the financial statements.

PNI continues to experience an erosion of its revenues from traditional one-way paging, which is the core of PNI's network services business and its principal revenue source. This decline in networking services revenue is indicative of the trends experienced by other one-way paging carriers. PNI expects to continue to experience significant net losses and declining cash flows. At the same time, the Company believes, based on information presently available to it, that cash available from its continuing operations will provide sufficient liquidity to allow it to continue as a going concern for the foreseeable future. However, the ability of the Company to continue as a going concern (including its ability to meet post-petition obligations of the Debtors) and the appropriateness of using the going concern basis for its financial statements are dependent upon, among other things, (i) the Company's ability to obtain sufficient credit and payment terms from vendors, (ii) the Company's ability to comply with the terms of any cash management order entered by the Bankruptcy Court in connection with the Chapter 11 cases, (iii) the ability of the Company to maintain adequate cash on hand, (iv) the ability of the Company to generate cash from operations, (v) confirmation of a plan of reorganization under the Bankruptcy Code, and (vi) the Company's ability to achieve profitability following such confirmation. As a result of these uncertainties, there can be no assurance that existing or future sources of liquidity will be adequate.

4. SUPPLEMENTAL CASH FLOW INFORMATION

Cash and cash equivalents include investments in money market instruments, which are carried at fair market

7

8

PNI TECHNOLOGIES, INC.  
(DEBTOR-IN-POSSESSION)

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
JUNE 30, 2001  
(UNAUDITED)

value. There were no significant federal or state income taxes paid or refunded for the six months ended June 30, 2001 and 2000.

5. IMPAIRMENT LOSS

Statement of Financial Accounting Standards ("SFAS") No. 121, Accounting For The Impairment Of Long Lived Assets and For Long Lived Assets To Be Disposed Of, requires impairment losses to be recognized

for long-lived assets used in operations when indicators of impairment are present and the undiscounted cash flows are not sufficient to recover the assets' carrying amount. The impairment loss is measured by comparing the fair value of the asset to its carrying amount. In accordance with SFAS 121, at June 30, 2001, a total impairment loss of \$20.1 million has been recorded relating to the write down of certain network system equipment in markets which the Company intends to discontinue service in the amount of \$6.2 million, the Company's intangible assets consisting of goodwill and FCC licenses in the amount of \$13.1 million, and for the write down of certain inventory in the amount of \$783,000. The network system equipment write down is based on limited market for the sale of this equipment to a third party, the declining financial condition of the Company's competitors, the declining number of paging subscribers industry-wide, and the overall level of excess network equipment in the industry. With respect to the intangibles, the value of these assets is directly attributable to the recurring revenue stream generated by the Company's customers. Due to recurring reductions in revenues and the number of active units in service, it is the opinion of management that the recoverability of the carrying value of these intangible assets may be in doubt. Further, the overall valuations in recent transactions involving other paging carriers and the current financial condition of the Company raise substantial questions concerning the recoverability of these assets. The impairment charge was taken at the time the Company made the decision to discontinue service to these markets, which was June 30, 2001.

#### 6. SEGMENT INFORMATION

The Company operates its business as one reportable segment.

8

9

PNI TECHNOLOGIES, INC.  
(DEBTOR-IN-POSSESSION)

#### ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

##### OVERVIEW

In this section, the Company makes reference to "EBITDA" which represents earnings before interest expense, interest income, taxes, depreciation and amortization. EBITDA is a financial measure commonly used in the telecommunications industry and should not be construed as an alternative to operating income (as determined in accordance with generally accepted accounting principles ("GAAP")), as an alternative to cash flows from operating activities (as determined in accordance with GAAP), or as a measure of liquidity. The table below provides the components of the Company's consolidated statements of operations and EBITDA for each of the three and six months ended June 30, 2001 and 2000, respectively, as a percentage of total revenues.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2001	2000	2001	2000
Revenues				
Network services .....	74.9%	72.1%	77.2%	74.1%
Pager sales .....	21.4	21.0	19.5	21.1
Networking products .....	2.5	5.0	1.9	3.4
Other services .....	1.2	1.9	1.4	1.4

Total revenues .....	100.0	100.0	100.0	100.0
Cost of revenues				
Network services .....	63.9	48.9	65.0	50.1
Pager sales .....	19.2	17.7	18.3	18.2
Networking products .....	5.3	3.0	5.8	2.7
Other services .....	0.0	0.0	0.0	0.0
Total cost of revenues .....	88.4	69.6	89.1	71.0
Gross margin .....	11.6	30.4	10.9	29.0
Selling, general and administrative expenses .....	81.0	43.0	67.1	42.2
Reorganization costs .....	2.7	--	1.3	--
Depreciation and amortization .....	50.2	33.6	49.3	33.6
Impairment loss .....	771.0	--	378.7	--
Operating loss .....	(893.3)	(46.2)	(485.5)	(46.8)
Interest expense .....	(5.8)	(4.3)	(5.7)	(4.3)
Interest income .....	0.0	2.0	0.1	1.3
Net loss .....	(899.1)%	(48.5)%	(491.1)%	(49.8)%
EBITDA .....	(843.1)%	(12.6)%	(436.2)%	(13.2)%

## RESULTS OF OPERATIONS

## Revenues

Total revenues were \$2.6 million and \$5.3 million for the three and six months ended June 30, 2001, respectively, compared to \$3.8 million and \$7.6 million for the three and six months ended June 30, 2000, respectively. The decrease in total revenues compared to the prior year periods was due to lower revenues in all revenue categories, with the largest decline occurring from network services.

Revenues from network services were \$2.0 million and \$4.1 million for the three and six months ended June 30, 2001, respectively, compared to \$2.7 million and \$5.6 million for the three and six months ended June 30, 2000, respectively. PNI's airtime revenues have been affected by industry trends of increased competition for reseller service units, declining service unit net additions and declining average revenue per unit ("ARPU"). The Company's airtime revenues were also affected by its limited working capital available for pager purchases,

PNI TECHNOLOGIES, INC.  
(DEBTOR-IN-POSSESSION)

because its customers typically rely on the Company for pager supply in order to add service units to the Company's networks. Due to these factors, PNI experienced a decline in total units in service to 348,179 at June 30, 2001, compared to 468,314 at June 30, 2000. In addition, total average revenue per unit ("ARPU") declined to \$1.82 for the six months ended June 30, 2001, compared to \$1.92 in the prior year period. As part of its planned reorganization under the Chapter 11 Bankruptcy filing, PNI intends to reduce its operating losses by discontinuing service in certain markets that are not profitable (consisting of its networks in the Mid-west, Florida, the Mid-Atlantic and selected networks operating on certain frequencies in the Southeast and Northeast.) PNI intends to continue to operate its profitable networks, which consist of the majority of its Northeast and Southeast operations. Accordingly, although PNI believes these efforts will provide a benefit to future net operating results, the reduction in network markets will result in a further decrease in units in services and

associated airtime revenues.

Revenues from pager sales were \$559,000 and \$1.0 million for the three and six months ended June 30, 2001, respectively, compared to \$791,000 and \$1.6 million for the three and six months ended June 30, 2000, respectively. PNI's pager sales were affected by its limited working capital available for pager purchases, as discussed above.

PNI began commercial shipments of its first networking product, the iTerminal(TM) desktop messaging terminal, in early 2000, and subsequently introduced additional products, including its Platform1(R) intelligent, high-speed, modular switch. PNI generated revenues from sales of networking products of \$66,000 and \$101,000 for the three and six months ended June 30, 2001 compared to \$189,000 and \$259,000 for the three and six months ended June 30, 2000. Due to the early stages of commercial sales of PNI's networking products, PNI's limited working capital, and PNI's limited development personnel, PNI has been inhibited in its ability to complete multiple customer orders. Concurrent with its Chapter 11 Bankruptcy filing, PNI suspended all development, assembly and shipments of its networking products. PNI does not expect to resume such activities in the foreseeable future, although it may seek to transfer or license its patent with respect to these technologies.

#### Cost of Revenues

Cost of network services was \$1.7 million and \$3.5 million for the three and six months ended June 30, 2001, respectively, compared to \$1.8 million and \$3.8 million for the three and six months ended June 30, 2000, respectively. The decrease in cost of network services is due to continued initiatives to reduce operating costs. Due to its plans to eliminate certain unprofitable network operations (as discussed above), PNI expects that it will achieve further reductions in cost of network services, consisting primarily of reductions in recurring site rents and telephone expenses.

Cost of pager sales were \$501,000 and \$972,000 for the three and six months ended June 30, 2001, respectively, compared to \$664,000 and \$1.4 million for the three and six months ended June 30, 2000, respectively. The decreases in cost of pager sales were due primarily to the Company's limited pager supply and related decrease in pager revenue.

Cost of networking products were \$137,000 and \$309,000 for the three and six months ended June 30, 2001, respectively, compared to \$112,000 and \$210,000 for the three and six months ended June 30, 2000, respectively. The majority of the cost of networking products in both periods resulted from an allocation of S,G&A expenses that are associated with the delivery of commercial products. Due to the early stages of commercial sales of PNI's networking products and its attempts to build its networking products business, this expense allocation exceeded the networking products revenues for both periods. In connection with the discontinuation of operations related to its networking products, this allocation will cease to occur in future periods.

#### Overhead

S,G&A expense was \$2.1 million and \$3.6 million for the three and six months ended June 30, 2001, respectively, compared to \$1.6 million and \$3.2 million for the three and six months ended June 30, 2000,

PNI TECHNOLOGIES, INC.  
(DEBTOR-IN-POSSESSION)

respectively. The increase in S,G&A expense was due primarily to a charge to bad debt expense during the three month period to write off certain outstanding accounts receivable that the Company believes may be uncollectable because of discontinuance of service in certain markets and due to additional accruals for

certain expenses that may be payable post-petition. Prior to this charge, the Company's S,G&A expenses would have decreased due primarily to reductions in personnel and office related expenses. Concurrent with its Chapter 11 Bankruptcy filing, PNI reduced its workforce by approximately 50% and commenced the consolidation of certain office operations, which will enable further reductions of personnel and office-related expenses in the future. Accordingly, PNI expects that its recurring S,G&A will further decrease. The Company also incurred approximately \$70,000 of reorganization costs for the three months ended June 30, 2001, consisting primarily of legal fees associated with the Chapter 11 Bankruptcy proceedings. Depreciation and amortization expense was \$1.3 million and \$2.6 million for the three and six months ended June 30, 2001 and 2000, respectively. Due to the write-down of certain assets (as further discussed below), the Company expects its depreciation expense to be reduced in future periods. Interest expense was \$151,000 and \$304,000 for the three and six months ended June 30, 2001 compared to \$162,000 and \$325,000 for the three and six months ended June 30, 2000.

Net loss before impairment loss was \$3.3 million and \$6.0 million for the three and six months ended June 30, 2001, respectively, compared to \$1.8 million and \$3.8 million for the three and six months ended June 30, 2000, respectively. The increase in net loss before impairment loss was due primarily to decreases in gross profit due to lower revenues and due to the charges to SG&A discussed above.

The net loss attributable to Common Stock was \$24.5 million and \$28.0 million for the three and six months ended June 30, 2001, respectively, compared to \$2.7 million and \$5.6 million for the three and six months ended June 30, 2000, respectively.

#### Impairment Loss

At June 30, 2001, a total impairment loss of \$20.1 million has been recorded relating to the write down of certain network system equipment in markets which the Company intends to discontinue service in the amount of \$6.2 million, the Company's intangible assets consisting of goodwill and FCC licenses in the amount of \$13.1 million, and for the write down of certain inventory in the amount of \$783,000. The network system equipment write down is based on limited market for the sale of this equipment to a third party, the declining financial condition of the Company's competitors, the declining number of paging subscribers industry-wide, and the overall level of excess network equipment in the industry. With respect to the intangibles, the value of these assets is directly attributable to the recurring revenue stream generated by the Company's customers. Due to recurring reductions in revenues and the number of active units in service, it is the opinion of management that the recoverability of the carrying value of these intangible assets may be in doubt. Further, the overall valuations in recent transactions involving other paging carriers and the current financial condition of the Company raise substantial questions concerning the recoverability of these assets.

#### Liquidity and Capital Resources

##### Summary of 2000 and 2001 Events

12

11

#### PNI TECHNOLOGIES, INC. (DEBTOR-IN-POSSESSION)

At June 30, 2001, PNI had \$1.2 million in cash, \$652,000 in net accounts receivable, \$3.6 million in accounts payable and \$1.3 million in accrued liabilities. An aggregate of \$5.3 million in principal plus accrued interest was outstanding under PNI's credit facilities with its lenders as of June 30, 2001. PNI's net cash used in operations for the six month period ended June 30, 2001 was \$593,000, compared to \$1.6 million in 2000. The reduction in cash used in operations was due primarily to the further aging of accounts

payable as part of the Company's efforts to preserve cash.

During the first six months of 2001, PNI continued in its efforts to develop its networking products business, and to that end incurred expenses in the development and promotion of this business that it would not have incurred solely as a provider of network services. PNI has not yet achieved significant sales of its networking products, and its costs attributable to this business have exceeded its revenues. Concurrent with its Chapter 11 Bankruptcy filing, PNI suspended all development, assembly and shipments of its networking products. PNI does not expect to resume such activities in the foreseeable future, although it may seek to transfer or license its patent with respect to these technologies. PNI's principal revenue source remains its network services business, which continues its trend toward lower per-user and aggregate revenues. PNI intends to reduce its operating losses by discontinuing service in certain markets that are not profitable (consisting of its networks in the Mid-west, Florida, the Mid-Atlantic and selected networks operating on certain frequencies in the Southeast and Northeast.). PNI intends to continue to operate its profitable networks, which consist of the majority of its Northeast and Southeast operations. Accordingly, although PNI believes that these efforts will provide a net benefit to future cash generation, the reduction in network markets will result in a further decrease in revenues.

PNI has three primary lenders, as further discussed in the "Capital Resources" section below. At June 30, 2001, PNI had \$1.9 million outstanding under a senior credit facility that is secured by substantially all of the assets of PNI and is to be used for working capital purposes. The amount outstanding under this facility was due on March 31, 2001. PNI notified this lender of its intent to delay this payment and of its efforts to complete a strategic transaction that would enable it to retire this obligation. In May 2001, this lender agreed to forbear its rights relating to the defaults during the period in which PNI hoped to consummate the strategic transaction. The Company does not presently believe that the anticipated strategic transaction will be consummated and management is no longer in discussions with this party.

Beginning in February 2001, PNI ceased to make principal and interest payments to its two other primary lenders, although these payments were due under the applicable loan agreements. These loans are secured by the majority of PNI's paging network assets. As of the date that PNI ceased to make payments to these institutions, the aggregate outstanding balance totaled \$3.3 million, of which \$1 million was due and payable on March 31, 2001. Thereafter, PNI is required to make regular principal payments to these lenders in the aggregate average monthly amount of \$180,000 (in addition to monthly interest payments) for the remainder of 2001. PNI notified these lenders of its intent to delay these payments and of its efforts to complete a strategic transaction that would enable it to retire these obligations. The Company does not presently believe that the anticipated strategic transaction will be consummated and management is no longer in discussions with this party.

#### Capital Resources

PNI continues to experience an erosion of its revenues from traditional one-way paging, which is the core of PNI's network services business and its principal revenue source. This decline in networking services revenue is indicative of the trends experienced by other one-way paging carriers. PNI expects to continue to experience significant net losses and negative cash flows. At the same time, the Company intends, under a plan of reorganization pursuant to its Chapter 11 Bankruptcy filing, to eliminate operations that are unprofitable and to continue to operate in network markets that are profitable. The Company believes, based on information presently available to it, that cash available from these continuing operations will provide sufficient liquidity to allow it to continue as a going concern for the foreseeable future. However, the ability of the Company to continue as a going concern (including its ability to meet post-petition obligations of the Debtors) and the appropriateness of using the going concern basis for its financial statements are dependent upon, among other things, (i) the Company's ability

PNI TECHNOLOGIES, INC.  
(DEBTOR-IN-POSSESSION)

to obtain sufficient credit and payment terms from vendors, (ii) the Company's ability to comply with the terms of any cash management order entered by the Bankruptcy Court in connection with the Chapter 11 cases, (iii) the ability of the Company to maintain adequate cash on hand, (iv) the ability of the Company to generate cash from operations, (v) confirmation of a plan of reorganization under the Bankruptcy Code, and (vi) the Company's ability to achieve profitability following such confirmation. As a result of these uncertainties, there can be no assurance that existing or future sources of liquidity will be adequate.

During 1999, the Company repaid in full its senior credit facility that was used to finance paging network acquisitions. At December 31, 1999, the Company had established a \$2.0 million revolving credit facility with this financial institution to be used for working capital purposes. The outstanding balance under this facility bears interest at 2% plus the prime rate. The amount outstanding under this facility as of June 30, 2001 was \$1.9 million, which was due on March 31, 2001. In May 2001, this lender agreed to forbear its rights relating to this and certain other defaults during the period in which PNI hoped to consummate the strategic transaction. However, the Company subsequently ceased to have discussions with this strategic party and did not meet the terms of the forbearance agreement, which constitutes an event of default. On July 10, 2001, the Company repaid \$364,000 of principal and accrued interest to this lender. Borrowings under this facility are secured by substantially all the assets of the Company. This credit facility contains various conditions, financial covenants and restrictions related to a variety of issues.

PNI has purchased certain of its paging network equipment under a vendor financing facility bearing interest at the rate of 12.57%. This credit facility was established in 1996 and this lender has since amended certain terms and conditions. This credit facility contains various conditions, financial covenants and restrictions and is secured by paging equipment. In connection with PNI's sale of its subsidiary EPS Wireless, Inc. in December 1999, this lender amended this facility with respect to the outstanding balance to suspend principal payments until March 31, 2001 (although PNI was still obligated to pay interest). A principal payment of \$1 million was due on March 31, 2001, following which PNI is obligated to make monthly principal payments of approximately \$124,000 until December 2001. As of June 30, 2001, there was \$1.9 million outstanding under this facility with no additional availability. PNI ceased to make interest payments to this lender in February 2001 and did not make the payment due on March 31, 2001, both of which constitute events of default. Since its Chapter 11 Bankruptcy filing, the Company has made no payments to this lender.

The Company has purchased certain of its paging network equipment under a secured credit facility from a finance company bearing interest at a rate of 10.0%. This credit facility was established in 1996 and this lender has since amended certain terms and conditions. This credit facility contains various conditions, financial covenants and restrictions and is secured by paging equipment. In connection with the sale of its subsidiary Preferred Technical Services, Inc., in May 1999, this lender amended this facility with respect to the outstanding balance to suspend principal payments until May 2000 (although the Company was still obligated to pay interest). In May 2000, a principal payment of \$613,000 was due and paid, following which monthly principal payments of approximately \$56,000 are due until February 2003. As of June 30, 2001, there was \$1.4 million outstanding under this facility with no additional availability. PNI ceased to make principal and interest payments to this lender in February 2001, both of which constitute events of default. Since its Chapter 11 Bankruptcy filing, the Company has made no payments to this lender.

In addition to the above-described issues related to PNI's

indebtedness, PNI's current financial situation could impact operations in a number of other ways, some, but not all, of which are described here. PNI continues to operate at a loss, and its current financial condition may adversely affect its ability to obtain supplies and services from vendors on acceptable terms, to maintain relationships with its existing vendors (in particular, its relationships with suppliers responsible for keeping PNI's networks operational), and to retain and attract employees and customers. These factors could, in turn, aggravate the condition PNI presently is experiencing by further reducing revenues and operating cash flow.

PNI may not be able to propose or have confirmed a plan of reorganization acceptable to creditors, or to

13

14

PNI TECHNOLOGIES, INC.  
(DEBTOR-IN-POSSESSION)

emerge from Chapter 11 Bankruptcy. If PNI was required to satisfy its obligations to its lenders, became insolvent or was liquidated, and PNI's lenders proceeded against PNI's assets to satisfy those obligations, the value of its assets might not be sufficient to satisfy those obligations. This condition could be exacerbated by the fact that some of PNI's assets are intangible assets, primarily FCC licenses, goodwill and subscriber lists. The Company believes its intangible assets in the context of a liquidation or sale of business will have substantially no value, and accordingly, the Company has written these assets down to \$0. At June 30, 2001, PNI's total tangible assets were approximately \$5.7 million. There can be no assurance that the value of PNI's assets is, or will be, sufficient to repay its debt obligations. Even if PNI is able to satisfy its debt obligations, this could exhaust most, if not all, of PNI's assets. In such a situation, there would be little, if any, surplus remaining for distribution to the holders of PNI's preferred and common stock.

Forward-Looking Statements

The Private Securities Litigation Reform Act of 1995 provides a "safe harbor" for forward-looking statements. Certain information included in this Quarterly Report on Form 10-Q, the Company's Annual Report on Form 10-K, and other materials filed or to be filed by PNI with the Securities and Exchange Commission (as well as information included in oral statements or other written statements made or to be made by PNI) contains statements that are or will be forward-looking, such as statements relating to future sales activity or financial performance, marketing efforts and their possible results, financing and restructuring alternatives and their possible results, the possibility of any reorganization, acquisition or other strategic transaction, future capital expenditures, financing sources and availability and the effects of laws and regulations (including FCC regulations) and competition. Such forward-looking information involves important risks and uncertainties that could significantly affect anticipated results in the future and, accordingly, such results may differ from those expressed in any forward-looking statements made by or on behalf of PNI. These risks and uncertainties include, but are not limited to, uncertainties affecting the wireless industries generally; risks relating to PNI's discontinuing service in certain markets; risks related principal suppliers discontinuing service to PNI due to the bankruptcy filing; risks relating to PNI's efforts to implement its business strategy, including successful completion of bankruptcy reorganization proceedings; risks related to loss of employees since PNI must retain a substantial number of employees to network services; the relatively unproven nature of PNI's networking products, which represent a new product line for PNI; challenges to PNI's technologies (such as challenges to the validity of the patent on PNI's switching technology); risks relating to the ability of PNI to obtain additional funds in the form of debt or equity (including availability of financing terms acceptable to PNI); fluctuations in interest rates; and the existence of and changes to federal and state laws and regulations.

## ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE OF MARKET RISK

There have been no significant changes since December 31, 2000. See Management's Discussion and Analysis of Financial Condition and Results of Operations.

## PART II

## ITEM 1. LEGAL PROCEEDINGS

The information called for by this item is provided in Note 3, Notes to Condensed Consolidated Financial Statements under Part I, Item 1 of this Form 10-Q, which discusses significant developments in the Bankruptcy proceedings involving the Registrant since the last Form 8-K filed by the company on June 8, 2001.

## ITEM 3. DEFAULTS UPON SENIOR SECURITIES

The Company has \$1.9 million outstanding under a revolving credit facility with a financial institution to be used for working capital purposes, which was due on March 31, 2001. PNI did not make this payment on March 31, 2001, which constitutes an event of default. In May 2001, this lender agreed to forbear its rights relating to this and certain other defaults until October 15, 2001, provided the Company makes a principal payment of \$500,000 by June 15, 2001. PNI did not make the principal payment on June 15, 2001, which constitutes an event of default.

14

15

PNI TECHNOLOGIES, INC.  
(DEBTOR-IN-POSSESSION)

The Company has purchased certain of its paging network equipment under a vendor financing facility that had \$1.9 million outstanding as of June 30, 2001. A principal payment of approximately \$1 million was due on March 31, 2001, following which PNI is obligated to make monthly principal payments of approximately \$124,000 until December 2001. PNI ceased to make interest payments to this lender beginning in February 2001 and did not make the payment due on March 31, 2001, both of which constitute events of default. A total of \$1.3 million in scheduled principal payments and \$103,000 of accrued interest was due and unpaid to this lender as of this filing date.

The Company has purchased certain of its paging network equipment under a secured credit facility that had \$1.4 million outstanding as of June 30, 2001. The Company is presently obligated to make monthly principal payments of approximately \$56,000 until February 2003. PNI ceased to make principal and interest payments to this lender beginning in February 2001, both of which constitute events of default. A total of \$275,000 in scheduled principal payments and \$56,000 of accrued interest was due and unpaid to this lender as of this filing date.

The filing of a voluntary petition for relief under the Bankruptcy Code constitutes a default under the Company's senior credit facilities.

## ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K.

## (a) Exhibits:

None

## (b) Reports on Form 8-K:

The Registrant filed a Form 8-K in connection with the Registrant's voluntary petition for reorganization under Title 11 of the United

States Code (the "Bankruptcy Code") United States Bankruptcy Court for the Northern District Court of Georgia (filed on June 8, 2001 and incorporated by reference herein).

15

16

PNI TECHNOLOGIES, INC.  
(DEBTOR-IN-POSSESSION)

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

PNI TECHNOLOGIES, INC.

Date: August 20, 2001 By: /s/ Mark B. Jones

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Mark B. Jones  
Chief Executive Officer, Chief Financial Officer and  
Principal Accounting Officer

16